SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1935

No. 824

JOSEPH H. BARWISE AND GEORGE THOMPSON, JR., AS TRUSTEES OF THE ESTATE OF MRS. M. M. (W. I.) COOK, DECEASED, APPELLANTS,

vs.

GEORGE H. SHEPPARD, AS COMPTROLLER OF THE STATE OF TEXAS, ET AL.

APPEAL FROM THE COURT OF CIVIL APPEALS, THIRD SUPREME JUDICIAL DISTRICT, STATE OF TEXAS

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[fol. 1]

IN DISTRICT COURT FOR THE 53rd JUDICIAL DISTRICT, TRAVIS COUNTY, TEXAS

No. 54,822

TRUSTEES OF MRS. M. M. (W. I.) COOK ESTATE,

vs.

GEORGE H. SHEPPARD, as Comptroller of the State of Texas, et al.

PLAINTIFFS' ORIGINAL PETITION—Filed Dec. 14, 1934

To said Honorable Court:

Come now Joseph H. Barwise, and George Thompson, Jr., as Trustees of the estate of Mrs. M. M. (W. I.) Cook, deceased, hereinafter designated plaintiffs, complaining of George H. Sheppard as Comptroller of Public Accounts of the State of Texas, and Charley Lockhart as State Treasurer of the State of Texas, hereinafter designated defendants, and for cause of action against said defendants, allege and would show to the Court as follows, to-wit:

I

(a) The plaintiffs are residents of Tarrant County, Texas.

(b) The defendants are residents of Travis County, Texas.

(c) The plaintiffs are the Trustees duly appointed, qualified and acting, under the will of Mrs. M. M. (W. I.) Cook, who died on or about February 22, 1932, and whose will was duly probated by an order of the County Court of Shackelford County, Texas, about April 5, 1932.

(d) The plaintiffs, under and by virtue of the terms and provisions of said will, became invested with and are the owners in fee simple of the lands, mineral rights and oil royalty interests therein, hereinafter described.

[fol. 2] (e) The defendant George H. Sheppard is the duly elected, qualified and acting Comptroller of Public

Accounts of the State of Texas; the defendant Charley Lockhart is the duly qualified and acting Treasurer of the State of Texas.

II

(a) Heretofore on or about the 11th day of May, 1925, Mrs. M. M. Cook, a widow, individually, and as independent executrix of the estate of W. I. Cook, her deceased husband, being the owner of the oil and gas in place under said land, made, executed and delivered to Roeser & Pendleton, Inc., two certain oil and gas leases covering, among other lands, Sections Nos. 60, 61, 62, 83, 84, 85 and 88, E. T. Ry. Co. Land in Shackelford County, Texas, being a part of what is generally known as the Cook ranch, by the terms of which the said Roeser & Pendleton, Inc., (lessee) acquired the right, exclusive of everyone, (including the lessor) to go upon, explore and develop said land for oil and gas, and by operations conducted thereon to produce and save oil and gas from said land, and, in consideration thereof contracted and agreed with lessor to deliver to the credit of lessor, (the said Mrs. M. M. Cook, her heirs or representatives) free of cost in the pipeline to which it might connect its wells, the equal 1/8th part of all oil produced and saved from the leased premises, as royalty oil.

(b) Since the execution of said leases there has been produced, from said land, approximately 11,000,000 barrels of oil, and there is now being produced therefrom approximately 2,000 barrels of oil per day.

(c) Plaintiffs, as trustees of the estate of Mrs. M. M. Cook, own one-half of the 1/8th oil royalty and royalty interest, under said land, in fee simple, and with respect to a small strip off the East side of sections 60, 61, 62 and the South side of sections 60, 85 and 88, a slightly larger proportion of the 1/8th royalty interest, as provided for in said leases. Plaintiffs believe and here so allege, that [fol. 3] there are yet in excess of 800,000 barrels of recoverable oil under said leased premises, of which more than 50,000 barrels, when produced and saved by the operating lessee, will belong to plaintiffs, as owners of the approximately 1/2 of the 1/8 Royalty interest, and they allege that the reasonable value of 2% of their interest in the oil royalty reserved, under said leases, is in excess of $1,000.00, and the one-half oil royalty interest owned by them there-

under (the title to which has been clouded as hereinafter set out) is reasonably worth in excess of $20,000.00.

III

(a) At the time of the execution of said leases, as aforesaid, producers and operators of oil properties in Texas, who are designated lessees, were required, by the then existing laws of Texas, to pay, from their share of the production of oil in the State of Texas, an occupation or privilege tax measured by a stated per centum of the total oil produced, including royalty oil.

(b) On the 22nd of May, 1933, there was approved by the Governor of the State of Texas, an Act of the Legislature of Texas, known as House Bill 154, Chapter 162, Acts 43rd Legislature, Regular Session (page 409) effective August 29, 1933, entitled:

"An Act to raise revenue for the support of the State Government by imposing and providing a tax upon the production of all oil within this State; * * * defining certain words, terms, and phrases for the purpose of this Act; providing the purchaser of oil shall pay the tax on oil purchased and deduct the tax so paid from the payment due the producer; providing the manner and method of remitting said tax to the Comptroller of Public Accounts and State Treasurer and requiring the tax to be paid on all oil that is not sold by the producer; providing for monthly payments of said tax and prescribing the date upon which tax shall be paid and by whom it shall be paid; providing that if said tax is withheld by the purchaser and said purchaser fails to make payment of said tax to the State that the producer may have legal action against the purchaser by reason of such failure, and providing for at- [fol. 4] torney's fees; providing for maintaining certain records; providing penalties for the failure to pay the tax imposed upon the production of oil and six per cent interest on delinquant penalties and interest; requiring the tax to be borne ratably by all interested parties; allocating the taxes received from all sources as herein imposed, * * * one-half to the Public School Fund and one-half to the credit of the General Revenue Fund, * * * requiring purchasers who buy oil from properties in litigation or covered by assignments to deduct amount of taxes before payment for said oil and to remit said tax deducted

in the same manner as provided for oil purchasers from other sources; requiring producers and purchasers to file certain reports with the Comptroller monthly and to submit said report with the amount of taxes due; providing that all taxes, penalties, and interest shall be secured by a first superior and preferred lien on the property of the producer, which shall include all leasehold interest and oil produced and all other property used in connection with the production of such oil; providing for the filing of suits by the Attorney General for the recovery of any taxes due or past due and providing for the venue for said suits in Travis County, Texas; providing that it shall be a misdemeanor for any person, firm, or corporation to violate any of the provisions of this Act and prescribing certain penalties as punishment for the violation of same by any producer, purchaser, * * * and the amount of expenses set out in said Act for the enforcement or administration be deducted from the gross amount collected monthly; * * * making it unlawful for any person owning, leasing, operating, or controlling any oil property to permit oil or gas to pass beyond his possession or control without first accurately measuring the amount of oil or gas and making and preserving an accurate record thereof and prescribing penalties for the violation thereof upon conviction; * * * providing that if any provision, section, or sub-section of this Act shall be held or declared to be unconstitutional for any reason, such decision or holding of the court shall not impair or affect any remaining portion of this Act, and the same shall remain in full force and effect and it is the intention of this Legislature that the same shall remain in full force and effect; and declaring an emergency."

(c) By section 1 of said Act, a "producer" is defined as meaning any person or persons, corporation, partnership, individual, trustee, receiver, trust estate or administrator owning, controlling, managing or leasing any oil well or any person who produces in any manner any oil by taking it from the earth or waters in the State. "Production of total oil produced" is defined as meaning 100% of [fol. 5] the oil produced in the State.

(* * * The omitted portions of the caption relate to taxes imposed on unrelated occupations.)

(d) By section 2 (1) of said Act there is levied an occupation tax, on oil produced within the State, of two cents (2¢) per barrel of 42 standard gallons. It is provided that said tax shall be computed upon the total oil produced, without deduction, and that the occupation tax levied shall be 2% of the market value of the oil whenever the market value exceeds $1.00 per barrel.

(e) By section 2 (2) it is provided that the tax levied shall be a liability of the producer; by section 2 (3) the purchaser of oil is required to pay the tax on all oil produced and to deduct the tax so paid from the payments due the "producer or other interest holder", such payments to be made to the Comptroller of Public Accounts by legal tender or cashier's check payable to the State Treasurer. It is provided, however, that if oil produced is not sold during the month produced then the producer shall pay the tax at the same rate and in the same manner as if the oil were sold.

(f) Section 2 (4) provides the time of payment of said tax, and section 2 (3) provides a penalty for delinquency of 10% of the amount of the tax and that the delinquent tax shall bear 6% interest per annum from due date until paid.

(g) Sevtion 2 (6) of said Act provides the tax therein levied shall be borne ratably by all interested parties, including royalty interest; and producers or purchasers of oil are thereby authorized and required to withhold, from any payments due interested parties, the proportionate tax due.

(h) Section 2 (7) directs the allocation of the tax by the Comptroller, ½ to the State Treasurer for the credit of the public school fund and ½ to the State Treasurer for the credit of the general fund of the State of Texas.

(i) Sections 3, 4, and 5 of said Act provide for the keeping of records, by producers and purchasers of oil, enable defendants to collect said tax from *difuciaries*, d pro-
[fol. 6] vide other administrative details relating to the collection and payment of the tax.

(j) Section 6 of said Act provides that, for the tax, penalty and interest, the State shall have a prior and preferred lien on any leasehold interest, ownership of oil rights, or interest, including oil produced and oil runs owned by the person owing such tax, and that such lien shall include

equipment, tools, tanks and all other implements used on the lease from which oil is produced.

(k) Section 9-B of said Act makes it a felony punishable by confinement in the penitentiary for from two to four years for any person owning, leasing, operating or controlling any oil property within the State of Texas to wilfully permit the oil or gas produced therefrom to pass beyond the possession or control of such person into the possession or control of such person into the possession or control of any other person without first accurately measuring the amount of such oil or such gas and making and preserving an accurate record thereof.

IV

The Act described in paragraph IV hereof, was amended at the first called session of the 43rd Legislature, 1933, (p. 43) by an Act entitled:

"An Act amending Sections 2, 3, 5 and 9 of Chapter 162, House Bill No. 154 Acts of the Forty-third Legislature, Regular Session, providing for monthly payment of tax levied and prescribing the date upon which tax shall be paid, by whom it shall be paid; providing that if said tax is withheld by the purchaser and said purchaser fails to make payment of said tax to the State that the producer may have legal action against the purchaser by reason of such failure, and providing for attorney's fee; providing penalties for the failure to pay the tax imposed upon the production of oil and six per cent (6%) interest on delinquent penalties and interest; providing the proceeds of said tax shall be deposited, one-half to the credit of the Public School Fund and one-half to the credit of the General Fund of the State of Texas; authorizing the Comptroller to promulgate rules and regulations for the enforcement of this Act and the amount of expenses set out in said Act for the enforcement or administration be deducted and appropriated from the gross amount collected, and providing for employees therein, prescribing maximum salaries, providing for equipment and supplies and other expenses necessary to enforce this Act, and declaring an emergency."

[fol. 7] This Amended Act, while re-enacting certain sections of the original law, in substance, changed the monthly

date for payment of the tax and the form of reports required thereby.

V

(a) Notwithstanding the fact that the plaintiffs are not producers, managers or operators of the oil property described herein, within the meaning of said Acts of the Legislature, and

(b) Notwithstanding the fact that, by the terms of the aforesaid leases, the lessee has the exclusive right to enter upon said land and explore, manage, develop and operate the same for oil and gas, and produce and save oil therefrom, being accountable to the plaintiffs for their aforesaid royalty oil; and

(c) Notwithstanding the fact that the plaintiffs are not engaged in an occupation or business in respect to the production of oil from said leases but are simply receiving and entitled to receive, under the terms of said leases, their royalty oil free of cost to them, in the pipeline to which the wells may be connected; and

(d) Notwithstanding the fact that while, the plaintiffs own an oil royalty interest, under said leases, they have no right or duty, under said leases to control the operation thereof or to produce oil from the lands covered thereby, or to take possession of and measure same, or any part thereof;

(1) Nevertheless, Plaintiff's allege: The defendant, the Comptroller of Public Accounts of the State of Texas, so plaintiffs are informed and believe, has notified the Humble Pipeline Company, the pipeline carrier of the oil produced from said leases, and the Humble Oil and Refining Company, the purchaser of the oil produced from said leases, and said lessee, that the part of said occupation tax imposed by said law, attributable to plaintiffs part of said [fol. 8] royalty oil, must be deducted from the amount due plaintiffs under said leases, and their contracts for the sale of said oil, and when so deducted, must be paid to said defendant, Comptroller of Public Accounts, pursuant to the provisions of said law, as amended, and that failure to pay the same will result in penalties being assessed against the plaintiffs, and as well the purchaser and transporter.

(2) Plaintiffs further allege, upon information and belief, that if said tax is paid out of plaintiff's money, said defendant, Comptroller of Public Accounts, upon receipt thereof, will turn the money over to the defendant State Treasurer for allocation as provided by said Act; and, unless such payments are made, in the manner aforesaid, the defendants, as required by said law, will cause suit to be instituted against plaintiffs, their lessees and the purchaser of their oil, to recover said tax, interest and penalties, and to foreclose the lien fixed by said Acts, upon plaintiffs oil royalty interest in said land.

(3) Plaintiffs further allege that since the enactment of said law the purchaser of said oil, Humble Oil and Refining Company, has deducted 2% of the value of plaintiffs oil, each month as and when produced by lessees, and has failed and refused, on account of said law, to pay plaintiffs 100% for their royalty oil, in accordance with plaintiff's contracts, and will continue to do so unless the relief prayed for herein is granted.

Plaintiffs would show to the Court that, as aforesaid, oil is being daily produced on the hereinbefore described lands in a large quantity, approximately (2,000 barrels per day), that the same is being daily sold and delivered; that the purchase price thereof is constantly accruing and becoming payable to the plaintiffs and under the provisions of said Act as amended, the purchaser or operator, as the case may be, is required to deduct from plaintiffs' royalty share of said oil and pay over to the Comptroller the two [fol. 9] cents per barrel or two per centum of the purchase price or value of said oil, to pay that part of the occupation tax of the lessee, who is exclusively operating the wells on plaintiffs' lands hereinbefore described.

(4) Plaintiffs further allege that the defendants, purporting to act under the terms of said Act, will continually and continuously during the pendency of this suit, unless restrained by order of this Court, attempt to interfere with and prevent the payment to the plaintiffs of the full 100% purchase price of their royalty oil, by having said tax deducted and paid over, as aforesaid.

(5) In this connection, the plaintiffs would show to the Court that long prior to the enactment of said law, they had a contract or contracts in writing with the above mentioned

pipeline carrier and purchaser of their royalty oil, produced from said land, by the terms of which the plaintiffs sold and agreed to deliver to the purchaser, through the instrumentality of said pipeline, the royalty oil belonging to them, produced from said leases premises, at and for the price posted from time to time by the purchasing for oil of like kind and quality, in the vicinity where the same was produced, and the purchaser agreed to pay the plaintiffs at stated times said posted price for such oil, without deduction, in compliance with said leases.

VI

Plaintiffs would show to the Court that said Acts of the Legislature, hereinbefore pleaded, violate the provisions of the Constitution of the United States and of the State of Texas in the following respects, to-wit:

(a) Said Acts violate the obligation of contract clauses of both the Federal and State Constitutions by appropriating, in violation of the lease contracts, aforesaid, between the plaintiffs and their lessees, a portion of the plaintiffs' royalty interest in said land perpetually, in the guise of collecting from plaintiffs a part of the occupation tax levied against the producer of said oil, the lessee, under said [fol. 10] leases.

(b) Said acts violate the obligation of contract clauses of both the Federal and State Constitutions by requiring the purchaser of said oil, or the producer as the case may be, in violation of the lease and oil purchase contracts, aforesaid, to pay over to the defendant State Comptroller, at least two per centum of the purchase price of said royalty oil, on account of the occupation tax levied against the occupation of the producers of said oil, the plaintiffs' lessees.

(c) Said Acts violate the due process of law clauses of both the Federal and State Constitutions by arbitrarily confiscating and appropriating perpetually as hereinbefore set forth, two per centum of the value of plaintiffs' oil Royalty interest in said lands, for the occupation tax liability of the producer of said oil.

(d) Said Acts of the Legislature are violative of the due process of law clauses of both the State and Federal Constitutions in arbitrarily and unreasonably requiring plain-

tiffs to bear at least two per centum of the occupation tax of another, to-wit: the producer, the plaintiffs are not being engaged in the business or occupation of producing oil.

(e) Said Acts are violative of the obligation of contract clauses of the State and Federal Constitution in creating and fixing a lien upon the plaintiffs royalty interest in said lands, for the entire tax, penalties and interest provided for in said acts, whereas, said leases imply, as aforesaid, that the plaintiffs' royalty interest shall be kept free of cost, charge or encumbrance on account of anything done by the producer in connection with the production of oil therefrom.

(f) Said Acts of the Legislature violate the due process of law clauses of both the State and Federal Constitutions in arbitrarily fixing a lien upon the plaintiffs' oil rights [fol. 11] under said leases and upon their oil produced therefrom or in transit, on account of the liability of the producer of said oil for said occupation tax, penalties and interest, thereby creating a cloud upon the plaintiffs' entire royalty interest in said leases on account of such unlawful and illegal provision.

(g) Said Act of May 22, 1933, is an original general Revenue measure. Theretofore an occupation tax had never been imposed upon royalty owners on account of the production of oil by the producer. The caption of said Act gives no notice, as is required by Article 3, Section 35, of the Texas Constitution, that a tax will be imposed by said Act directly or indirectly upon the owners of oil royalty or upon the property of oil royalty owners. The amendatory Act, aforesaid, is violative of said Constitutional provision for the same reason.

VII

The defendants have interpreted said Act of the Legislature as imposing an occupation tax upon producers of oil and as requiring the owners of royalty to pay a portion of such occupation tax, all as hereinbefore alleged, and in the light of such interpretation are applying the same against the plaintiffs and others similarly situated, unlawfully and in violation of plaintiffs' constitutional rights in each of the respects hereinbefore set forth.

VIII

In truth and in fact, notwithstanding the foregoing facts said Acts cannot be construed otherwise than as a tax upon the plaintiffs' oil royalty interest under said leases and lands as such, and same are violative of the Constitution of Texas in this:

(b) Plaintiffs allege that under the Constitution and laws of the State of Texas their interest in said property [fol. 12] is and constitutes realty, taxable as such, in and by the County where it is situated, and as other real property, solely according to its value, equally and uniformly with other property, at a rate not in excess of 35¢ on the $100.00 valuation and the Commissioners' Court of the several counties are the sole authorities authorized to fix such value.

(c) In this connection plaintiffs allege that they have duly paid and have been assessed by the tax assessor of Shackelford County, Texas, for State and County taxes on account of said oil royalty interest, in the manner provided by law.

(d) That no other real property in said County or in the State is assessed on an ad valorem basis, and at the same time upon a basis similar to that imposed upon it by the Acts in question, so that said Acts impose a double tax upon the plaintiffs property, in violation of (1) the equal and uniform tax clauses contained in Section 1, Article 8, of the Texas Constitution; (2) the 35¢ on the $100.00 valuation clause of Section 9, Article 8, of the Texas Constitution; (3) the provisions of the Constitution of Texas relating to the rendition and assessment of land in the County where situated, and (4) the provisions relating to the valuation thereof for tax purposes, by the Commissioners' Court.

IX

Heretofore on April 6, 1934, these plaintiffs sued the defendants and the Attorney General of Texas in the District Court of the United States for the Western District of Texas, at Austin in Cause No. 479 Equity, on the same grounds set forth herein but on motion of the defendant said cause was dismissed without decision, as, it was held,

the amount in controversy was not sufficient to give said Court jurisdiction. On that account however the defendant [fol. 13] Comptroller has been considering the money paid by the Humble Oil & Refining Company as gross production tax attributable to plaintiffs' interest aforesaid, as in litigation and has held the same in suspense and the same has not been commingled with other funds of the State. In this connection plaintiffs allege that unless restrained the defendants will unlawfully cause said money to be taken out of said suspense account and commingled with other funds of the State and therefore lost to the plaintiffs. The amount of money so in suspense in the hands of the defendants is to-wit: the sum of $1,000.00, but the exact amount thereof is peculiarly known to the defendant.

X

The plaintiffs have no plain, adequate and speedy remedy at law for the protection of their rights in the premises, because:

(1) The laws in question are new and have not been interpreted by our Courts.

(2) The taxes in question are not paid by the plaintiffs but are charged to them and paid by the purchaser of the oil or the producer as the sace may be, in the manner hereinbefore specified. Upon payment thereof into the hands of the defendants Comptroller and State Treasurer, there is no law authorizing the recovery of the same back and such monies pass into the general funds of the State, save that

(3) The only remedy at law, which plaintiffs allege is inadequate, is that provided by House Bill No. 11, Chapter 214, Acts 43rd Legislature, Regular Session (p. 637) which authorizes only such persons as are required by law to pay occupation, franchise, license or privilege taxes, to pay the same under protest, if they believe the tax is unlawful and such taxpayer has 90 days from date of payment to sue for the recovery of the tax paid, in the District Court of Travis County, and nowhere else.

[fol. 14] (4) Monies paid on such accounts under protest are to be held by the defendant State Treasurer in suspense and deposited at interest with other State funds and

the same are required when deposited, to earn interest in the depository, at the same rate as other State funds. Plaintiffs allege the amount of such earned interest is less than common interest of 6% and is wholly inadequate to recompense the plaintiffs for the loss of the use of said money during the suit period.

(5) The remedy, provided by said law, limits the recovery to the amount paid plus the earned interest.

(6) By virtue of said Act, also, protesting taxpayers are limited in their suit to the recovery of only such taxes as were paid under protest and to the grounds specified in the protest.

(7) There is no provision of State law for the impounding of monies paid on account of said tax after the institution of said suit so that successive monthly protests and actions under said law would be necessary to protect the rights of the protesting taxpayer during the period the law was being tested.

(8) It is certain that the remedy provided by said law cannot be invoked by the plaintiffs, as they are not, within the terms thereof, taxpayers and are not authorized to make the protest and bring the suit provided for therein.

(9) Said law was approved and made effective June 7, 1933, and has not been interpreted by the highest courts of Texas.

(10) As plaintiffs do not personally pay said tax, and have no control over those paying the same for their account, they cannot refuse payment thereof and defend a suit by the State to recover the same, and even if they could the excessive penalty for testing the law, coupled with the clouding of their title, as it does, would be prohibitive.

Wherefore, premises considered, plaintiffs pray that a temporary injunction be granted herein enjoining the defendants and each of them from interfering with the con- [fol. 15] tractual relations between the plaintiffs, their lessees, and the purchasers of their royalty oil, by demanding or collecting said tax on such oil, and requiring, pending final hearing hereof, all monies in or coming into the hands of the defendants as the two per centum gross pro-

duction tax charged, demanded and collected from royalty oil, of plaintiffs to be impounded and not paid or put to the credit of the funds of the state, but be held for the use and benefit of the plaintiffs, and enjoining the defendants, and each of them, from demanding any part of said gross production tax attributable to royalty oil of the plaintiffs, and that on final hearing said temporary injunction to be made permanent and the cloud cast on the title of plaintiffs' oil royalty interest in the lands hereinbefore described and by virtue of the lien sought to be fixed thereon by said laws, be cancelled and annulled; that the defendants be required to account to the plaintiffs for the money in or coming into their hands as or for account of said unlawfully charged gross production tax, levied against plaintiffs said royalty, and on such accounting that they have judgment against the defendants for the amount ascertained to have been withheld from them, with 6% interest thereon; and, that the plaintiffs have all such other and further relief in the premises both general and special to which they may be entitled, in law or in equity.

William R. Watkins, Attorney for the Plaintiffs.

Duly sworn to by George Thompson, Jr. Jurat omitted in printing.

[fol. 16] In Chambers, this the 14th day of Dec. 1934

Upon consideration of the foregoing petition, it is ordered that the Plaintiff's Application for Temporary Injunction be and the same is hereby set for Jan. 7, 1935, at 9 A. M.

C. A. Wheeler, Judge, 53rd Judicial District of Texas.

[File endorsement omitted.]

[fol. 17] IN DISTRICT COURT OF TRAVIS COUNTY

[Title omitted]

DEFENDANTS' ORIGINAL ANSWER—Filed Jan. 24, 1935

To the Honorable Judge Presiding:

Come now the defendants in the above numbered and entitled cause and file their answer to plaintiffs' Original Petition and for answer to same:

I

Defendants demur generally to plaintiffs' petition and say that the same states no ground for relief, of which general demurrer defendants pray judgment of the Court.

II

Without waiving the foregoing demurrer, but still insisting on same, defendants deny all and singular the allegations contained in plaintiffs' petition except those allegations constituting substantially the stipulations of fact signed by attorney for the plaintiffs and defendants and filed with the Court.

Wherefore, defendants pray that the temporary injunction heretofore granted by this Honorable Court be dissolved, and that plaintiffs take nothing and have no relief by their suit.

Hubert T. Faulk, Assistant Attorney General, Attorney for Defendants.

[File endorsement omitted.]

[fol. 18] IN DISTRICT COURT OF TRAVIS COUNTY

[Title omitted]

Portions of Agreed Statement of Facts—Filed Feb. 23, 1935

STIPULATION

For the purpose of the hearing on the application of the plaintiffs for an interlocutory and permanent injunction,

the parties to the above entitled and numbered cause agree that the following facts are true:

* * * * * * *

II

Thereafter the defendant, Comptroller, pursuant to the terms of said law authorizing him to make rules and regulations promulgated rules and regulations and forms of reports as follows:

* * * * * * *

(1) All purchasers of crude oil are required to file forms No. 100 (hereinafter described). They shall pay the tax upon purchases and are required to deduct such tax in making settlement with the producers and/or royalty owners.

* * * * * * *

The producer must report the gross production from each lease operated, regardless of the interest holders and royalty interests.

* * * * * * *

(6) The producer must report that oil which he delivers to the royalty owner for his share of the production commonly known as "payment in kind." The purchaser or royalty owner receiving such oil will report and remit the tax on the oil which has been received in payment on his royalty interests.

* * * * * * *

[fol. 19] (d) The Comptroller has prescribed form No. 200, above mentioned, being the monthly report required from producers and which may be described as follows:

(1) "The name and address of the producer and period covered by the report must be shown.

* * * * * * *

(3) It is recited that producer must remit the tax on all oil stored or used.

* * * * * * *

(6) The following page of the report requiring computations to be made on the basis of 100% of the gross production requires a showing of the name and address of purchaser, County and name of lease in which produced, gross production, disposition and location of storage of the oil, both in barrels and by value.

* * * * * * *

(8) Under the "Instructions," the producer is further required to remit the tax on all oil placed in storage and not sold during the month covered by the report, and also on oil consumed in the operation or on the lease during the month.

(9) Under the heading "Instructions" on said form is the following paragraph:

"The producer is liable for a fine of not less than $25.00 nor more than $5,000.00 or confinement in the county jail for not less than one month nor more than six months or by both such fine and imprisonment for the failure to file forms 200, or 202 at the time prescribed by law."

(e) Forms Numbers 100 and 200, last above described, the rules and regulations under the heading "Instructions" on said forms; and the General Rules and Regulations promulgated pursuant to said House Bill No. 154, hereinbefore described, are now in full force and effect.

* * * * * * *

[fol. 20] IV

The Humble Oil & Refining Company, as producer thereof, has protested the payment of the gross production tax upon the royalty oil produced by Roeser & Pendleton, Inc., or its assigns, from the Cook ranch in Shackelford County, Texas, being the property mentioned in plaintiff's petition, in which the Mrs. M. M. Cook estate trustees plaintiffs herein, own substantially a one-half (½) royalty interest under the leases thereon as hereinafter stated; said protest being in each instance substantially as follows:

"House Bill 154 is invalid insofar as it attempts to impose a tax upon royalty and/or working interests of the

parties listed above and reflected in the statement mentioned in paragraph (7) hereof, for the following reasons:

"(1) Because the caption of the act is not sufficiently broad to authorize and justify the treatment in one Act of the subjects attempted to be covered.

"(2) Because the caption of the Act and the Act itself deals with two or more separate and distinct subjects, in violation of the constitution of the State of Texas.

"(3) Because the Act is property tax and not a tax imposed upon the business of engaging in the production of oil or producing oil.

"(4) Because the Act contains contradictory and ambiguous provisions.

"(5) Because the Act imposes upon the producer or purchaser the duty and responsibility of acting as agent for the State in the collection of the tax; makes him liable for the tax to the State; requires him to take from others property not belonging to him, and subjects him to a measure of liability which he cannot be required to assume; requires him to incur accounting and other expense in the collection of the tax, all without compensation, and in violation of the State and Federal prohibition against the taking of property without due process of law and the denial of the equal protection of the law.

"(6) Because, as to the royalty interests, the royalty owner is not engaged in the production of oil, and the tax attempted to be imposed cannot be justified as an occupation tax.

"(7) Because the Act attempts to abrogate vested contractual rights."

* * * * * * *

[fol. 21] VIII

On behalf of the plaintiffs in this case, the Humble Oil & Refining Company, the purchaser of plaintiffs' royalty oil, protested the payment and deduction of two (2%) per cent from the amounts due plaintiffs for the sale of their royalty oil to said Company on the form hereinabove men-

tioned, said protests covering the months and the amounts following:

December 1933	$52.30
January 1934	76.21
February	71.71
March	83.80
April	88.01
May	87.60
June	84.30
July	91.22
August	92.13
September	89.64
October	90.30

Pursuant to the foregoing protests, all of the money affected hereby has been delivered by the Comptroller to the State Treasurer and by the latter deposited and held in suspense account.

* * * * * * *

X

Mrs. M. M. (W. I.) Cook, of Albany, Shackelford County, Texas, during the year 1934 and up to her death on February 22, 1932, was the owner of the W. I. Cook Ranch, in Shackelford County, Texas, consisting of approximately 20,021 acres of land.

On May 11, 1925, Mrs. Cook executed, acknowledged and delivered, as lessor, to Roeser & Pendleton, Inc., a corporation, as lessee, three (3) oil, gas and mineral leases, identical in form, each dated May 11, 1925—Lease No. 1 covering 5,773 acres out of the Cook Ranch (including Sections 62 and 83 of the E. T. R. R. Co. Land)—Lease No. 2 covering 6,400 acres of land out of the Cook Ranch (including Sections 60, 61, 84, 85 and 88 of the E. T. R. R. Co. Land)—Lease No. 3 covering 5,760 acres of land out of the Cook Ranch. A copy of oil, gas and mineral Lease No. 2 is [fol. 22] attached hereto as Exhibit 1, and the terms and provisions of same are identical with the terms and provisions of Leases Nos. 1 and 3 mentioned.

Roeser & Pendleton, Inc., lessee named in said three oil, gas and mineral leases above referred to, drilled a dis-

covery well upon Section 60, E. T. R. R. Co. Land, and same was brought in as a producer on the 19th day of February, 1926. Following completion of this discovery well, Roeser & Pendleton, Inc., drilled over 400 wells on Sections 60, 61, 62, 83, 84, 85 and 88 of E. T. R. R. Co. Land on the Cook Ranch in Shackelford County, Texas, each of said wells being drilled to an approximate depth of 1,250 feet.

EXHIBIT I

Oil and Gas Lease 2830

Agreement, made and entered into the 11th day of May, 1925, by and between M. M. Cook for myself and as Independent Executrix of the Estate of W. I. Cook, deceased, of Albany, Texas, hereinafter called lessor (whether one or more), and Roeser and Pendleton, Inc., hereinafter called lessee:

Witnesseth: That the said lessor, for and in consideration of Six Thousand Four Hundred and No/100 ($6,400.00) Dollars, cash in hand paid, the receipt of which is hereby acknowledged, and of the covenants and agreements hereinafter contained on the part of lessee to be paid, kept and performed, have granted, demised, leased and let, and by these presents does grant, lease and let unto the said lessee for the sole and only purpose of mining and operating for oil and gas and of laying pipe lines and of building tanks, power stations and structures thereon to produce, save and take care of said products, all that certain tract of land situated in the County of Shackelford, [fol. 23] State of Texas, containing 6,400 acres, more or less, and described as follows, to-wit:

First Tract: Being Section No. 61, E. T. Ry. land, containing 640 acres.

Second Tract: Being Section No. 60, E. T. Ry. land, containing 640 acres.

Third Tract: Being Section No. 84, E. T. Ry. land, containing 640 acres.

Fourth Tract: Being Section No. 85, E. T. Ry. land, containing 640 acres.

Fifth Tract: Being Section No. 88, E. T. Ry. land, containing 640 acres.

Sixth Tract: Being Section No. 89, E. T. Ry. land, containing 640 acres.

Seventh Tract: Being Section No. 90, E. T. Ry. land, containing 640 acres.

Eighth Tract: Being Section No. 111, E. T. Ry. land, containing 640 acres.

Ninth Tract: Being Section No. 112, E. T. Ry. land, containing 640 acres.

Tenth Tract: Being Section No. 113, E. T. Ry. land, containing 640 acres.

Said ten tracts above described, containing in the aggregate 6,400 acres.

It is understood and agreed that an individed ½ interest of the oil and gas in and under the E. ½ of Sec. No. 60, above described has been heretofore conveyed by the fee owner to T. B. Owen and it is agreed that the lessee its heirs and assigns, shall be entitled to receive ⅞ of all the oil and gas in and under the E. ½ of said Section No. 60, and that said ⅛ of said oil and gas heretofore conveyed shall be delivered or paid from the ⅛ royalty reserved in this lease.

It is also understood and agreed that an undivided 1/16 interest to the oil and gas in and under Section No. 89 [fol. 24] E. T. Ry. Company land, containing 640 acres above described has been heretofore conveyed by the fee owner to S. Granman, and it is agreed that the lessee its assigns and successors shall be entitled to receive ⅞ of all the oil and gas in and under said Section No. 89, and said 1/16 of said oil and gas heretofore conveyed shall be delivered or paid from the ⅛ royalty from this lease.

It is further understood and agreed that an undivided 1/16 interest in the oil and gas in and under the E. ½ of section No. 111, above described containing 320 acres, has been heretofore conveyed to T. B. Owen, and that it is agreed that the lessee its assigns and successors shall be entitled to receive ⅞ of the oil and gas in and under the E. ½ of said Section No. 111, and that said 1/16 interest of said oil and gas heretofore conveyed shall be delivered or paid from the ⅛ royalty reserved in this lease.

It is also further understood and agreed that an undivided 1/16 interest of the oil and gas in and under the W. ½ of Section No. 112, E. T. Ry. Co. above described, containing 320 acres of land, has been heretofore conveyed

to Roy B. Jones, and it is agreed that the lessee its assigns and successors shall be entitled to receive 7/8 of all the oil and gas in and under said W. 1/2 of said Section No. 112, and that the said 1/16 interest of said oil and gas heretofore conveyed shall be delivered or paid from the 1/8 royalty reserved in this lease.

It is also further agreed and understood that an undivided 1/16 interest of the oil and gas in and under the E. 1/2 of Section No. 112 E. T. Ry. Co. above described, containing 320 acres of land has been heretofore conveyed by the fee owner to W. L. Thomas and it is agreed that the lessee its assigns and successors shall be entitled to receive 7/8 of all the oil and gas in and under the E. 1/2 of said Section No. 112 and that said 1/16 interest of said oil and gas heretofore conveyed shall be delivered or paid from [fol. 25] the 1/8 royalty reserved in this lease.

It is further understood and agreed that an undivided 1/16 interest of the oil and gas in and under Section No. 113, E. T. Ry. Co. above described containing 640 acres of land, has been heretofore conveyed to P. W. Reynolds, and it is agreed that the lessee its assigns and successors shall be entitled to receive 7/8 of all the oil and gas in and under said Section No. 113, and that said 1/16 interest of said oil and gas heretofore conveyed shall be delivered or paid from the 1/8 royalty reserved in this lease.

It is agreed that this lease shall remain in force for a term of five years from this date, and as long thereafter as oil or gas, or either of them is produced from the said land by the lessee.

In consideration of the premises the said lessee covenants and agrees:

1st. To deliver to the credit of lessor, free of cost, in the pipeline to which it may connect its wells, the equal one-eighty part of all oil produced and saved from the leased premises.

2nd. To pay the lessor 1/8 of the proceeds of such gas for the gas from each well where gas only is found, while the same is being used off the premises, and lessor to have gas free of cost from any such well for all stoves and all inside lights in the principal dwelling house on said land during the time by making her own connections with the well at her own risk and expense.

3rd. To pay lessor for gas produced from any oil well and used off the premises at the rate of 1/8 of the proceeds of all such gas for the time during which such gas shall be used. Also 1/8 of the proceeds of casing head gas.

If no well be commenced on said land on or before the 11th day of May, 1926, this lease shall terminate as to both parties, unless the lessee on or before that date shall pay or render to the lessor, or to the lessor's credit in the First [fol. 26] National Bank at Albany, Texas, or it- successors, which shall continue as the depository, regardless of changes in the ownership of said land, the sum of Sixteen Hundred and No/100 ($1,600.00) Dollars, which shall operate as rental and cover the privilege of deferring the commencement of a well for twelve months from said date. In like manner and upon like payments or tenders the commencement of a well may be further deferred for like periods of the same number of months successively. And it is understood and agreed that the consideration first recited herein, the down payment, covers not only the privilege granted to the date when said first rental is payable as aforesaid, but also the lessee's option of extending that period as aforesaid, and any and all other rights conferred.

Should the first well drilled on the above described land be a dry hole, then and in that event, if a second well is not commenced on said land within twelve months thereafter, this lease shall terminate as to both parties, unless the lessee on or before the expiration of said twelve months shall resume the payments of rentals in the same amount and in the same manner as hereinbefore provided. And it is agreed that upon the resumption of the payments of rentals, as above provided, that the last preceding paragraph hereof, governing the payment of rentals and the effect thereof, shall continue in force just as though there had been no interruption in the rental payments.

If said lessor owns a less interest in the above described land than the entire and undivided fee simple estate therein, then the royalties and rentals herein provided for shall be paid the said lessor only in proportion *with* interest bears to the whole and undivided fee.

Lessee shall have the right to use, free of cost, gas, oil and water produced on said land for all operations thereon, except water wells of lessor.

[fol. 27] When requested by lessor lessee shall bury all pipe line below plow depth.

No well shall be drilled nearer than 200 feet to the house or barn now on said premises without the written consent of the lessor.

Lessee shall pay for damages caused by all operations to growing crops on said land.

Lessee shall have the right at any time to remove all machinery and fixtures placed on said premises, including the right to draw and remove casing.

If the estate of either party hereto is assigned—and the privilege of assigning in whole or in part is expressly allowed—the covenants hereof shall extend to their heirs, executors, administrators, successors, or assigns, but no change in the ownership of the land or assignment of rentals or royalties shall be binding on the lessee until after the lessee has been furnished with a written transfer or assignment, or a copy thereof; and it is hereby agreed that in the event that this lease shall be assigned as to a part or as to parts of the above described lands and the assignee or assignees of such part or parts shall fail or make default in the payment of the proportionate part of the rents due from him or them, such default shall not operate to defeat or affect this lease so far as it covers a part or parts of said lands upon which the said lessee or any assignee thereof shall make due payment of said rental.

Lessor hereby warrants and agrees to defend the title to the lands herein described and agrees that the lessee shall have the right at any time to redeem for lessor, by payment, any mortgages, taxes, or other liens on the above described lands, in the event of default of payment by lessor, and be subrogated to the rights of the holder thereof.

It is understood that this lease is No. 2 of a series of three leases this day executed by and between the parties hereto, and in the event lessee shall drill a well on any of [fol. 28] said land, and produce and deliver in a pipeline on said lease or leases as much as ten barrels per day of oil for a period of thirty days in succession then and in such event such production shall operate to stop the payment of any further rentals on the lands, described in this lease in Nos. 1 and 3, which are companion leases to this one.

In testimony whereof, we sign, this the 11th day of May, 1925.

M. M. Cook, for Herself and as Independent Executrix of the Estate of W. I. Cook, Deceased.

Single Acknowledgment

THE STATE OF TEXAS,
County of Shackelford:

Before me, the undersigned authority, a Notary Public in and for the County of Shackelford and State of Texas, on this day personally appeared M. M. Cook, for herself and as independent executrix of the Estate of W. I. Cook, deceased, known to me to be the person whose name is subscribed to the foregoing instrument, and acknowledged to me that she executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office on this the 22nd day of June, A. D. 1925.

R. E. Dodge, Notary Public in and for Shackelford County, Texas. (L. S.)

THE STATE OF TEXAS,
County of Shackelford:

I, W. Floyd Jones, County Clerk in and for said County, do hereby certify that the foregoing instrument dated the 11th day of May, A. D. 1925, with its certificate of authentication, was filed for record in my office, the 23rd day of June, A. D. 1925, at 11:00 o'clock A. M., and duly recorded the 24th day of June, 1925, in the records of said County, [fol. 29] in Vol. 77 on page 42.

Witness my hand and the seal of the County Court of said County, at office in Albany, Texas, the day and year last written.

W. Floyd Jones, Clerk County Court, Shackelford County, Texas.

Compared 1161 Indexed

Producer's 88 Special

Lease No. 2

Oil and Gas Lease from M. M. Cook to Roeser and Pendleton, Inc.

This instrument was filed for record on the 23rd day of June, 1925, at 11:00 o'clock A. M., and duly recorded in Book —, page — of the — records of this office.
W. Floyd Jones, County Clerk, by —— ——, Deputy.

XI

Mrs. Cook, as stated, died on February 22, 1932, and her will was probated in the County Court of Shackelford County, Texas. George Thompson, Jr., and R. E. Nail were named as Independent Executors. R. E. Nail died in September, 1932, and since that date, George Thompson, Jr. has acted as sole Independent Executor, until September 1, 1933, when the executorship was closed and the Trust Estate established under Mrs. Cook's will commenced. Since September 1, 1933, Joseph H. Barwise and George Thompson, Jr., Trustees of Mrs. Cook's Estate, have been and are now the owners in fee of the oil, gas and mineral royalty reserved by Mrs. Cook in the oil and gas leases hereinbefore mentioned with the exception of the one-fourth of said royalty given by Mrs. Cook in 1927 to the W. I. Cook Memorial Hospital, and an additional one-fourth which she [fol. 30] gave to said Hospital upon her death, and with the further exception of the small outstanding fractional interests in two or three of the sections. In other words, Joseph H. Barwise and George Thompson, Jr., Trustees, since September 1, 1933, have been and are now the owners of substantially one-half of the royalty reserved by Mrs. Cook in said oil, gas and mineral leases mentioned.

XII

Roeser & Pendleton, Inc., and its assigns, have had the exclusive control and operation of the oil, gas and mineral

development and production of oil from the Cook Ranch, and that at no time has either Mrs. W. I. Cook or the Trustees of her estate ever exercised, or attempted to exercise, any degree of control over oil operations on said Cook Ranch; and at no time has either Mrs. Cook or the Trustees of her estate ever produced any oil from the Cook Ranch, or ever been in the occupation of producing oil from the Cook Ranch, but on the contrary Roeser & Pendleton, Inc., and its assigns, have been the sole and exclusive producers of oil and gas from said Cook Ranch, and no other person, save Roeser & Pendleton, Inc. and its assigns, has been engaged in such occupation named. In connection with the foregoing, and in using the phrase, "Roeser & Pendleton, Inc., and its assigns," it is meant to include in said term the assigns of Roeser & Pendleton, Inc., but neither Mrs. Cook nor the Trustees of her estate, has been such assigns, but they have at all times been merely the owner of substantially one-half of the royalty oil produced from the Cook Ranch by Roeser & Pendleton, Inc., lessee and its assigns.

* * * * * * *

XIV

That on September 1, 1933, the Humble Oil & Refining Company was purchasing all of the oil produced from [fol. 31] said Cook Ranch, including the substantially one-half oil royalty owned by the Trustees of Mrs. Cook's Estate, upon written Division Orders, all identical in form, but varying as to percentage of interest, a copy of one of said Division Orders being attached hereto and marked Exhibit 2. Under said Division orders, said Humble Oil & Refining Company had been paying to the Trustees of Mrs. Cook's estate, and continued to pay, until 2% gross production tax law (mentioned in plaintiffs' petition) went into effect, the full market value and posted price for said oil, without deduction except for a small allowance for basic sediment, as provided for in the Division Orders.

EXHIBIT 2

Humble Oil & Refining Company

Division Order No. 2107

Effective 7 A. M. February 1, 1932

To Humble Oil & Refining Co., Houston, Texas:

The undersigned certify and guarantee that they are the owners of the oil, including royalty interest, produced from wells, No. 1 and up, on the W. I. Cook farm or lease, in Oil Field in Shackelford County, Texas, which farm or lease is described as follows:

All of the N. ½
N. ½ of S. W. ¼
N ½ of the S. E. ¼ and
S. W. ¼ of S. E. ¼ of Section 84,
E. T. R. R. Co. Lands,
Abstract No. 1388.
Shackelford County, Texas.

Until further written notice, you are authorized, for your own account, to receive such oil into your own possession or the possession of any person or corporation designated by you, same to be run and measured in accordance with the customary pipeline rules and regulations, including adjustments and deductions provided for by the [fol. 32] rules of the Texas Railroad Commission, such oil to be credited as follows:

Credit to W. I. Cook Memorial Trust; Division of Interest ½ of ⅛; Postoffice Address, Fort Worth, Texas.

Credit to R. E. Nail & Geo. Thompson, Jr.; Independent Executors and Trustees Mrs. W. I. Cook Estate; Division of Interest ½ of ⅛; Postoffice Address, Albany, Texas.

The oil run hereunder shall on the terms herein contained become the property of Humble Oil & Refining Company immediately upon being received into the possession of said Company or its designated agent, and said Company agrees to receive and pay for such oil to the respective owners according to the division of interest hereinabove indicated at its posted per barrel (42 gallons) field price for similar crude in the field where received prevailing on the

date of each respective run, settlements, and payment to be made monthly by check of Humble Oil & Refining Company mailed to the respective parties at the addresses above given.

Each undersigned hereby warrants and guarantees the title to the oil credited to such undersigned owner according to the division of interest hereinabove indicated, as well as all interest hereafter acquired and agrees to furnish abstract of title, and in case of any adverse claim of title to such oil or any part thereof, or to the land from which such oil is produced to furnish Humble Oil & Refining Company satisfactory indemnity bond against such adverse claim or claims and to authorize Humble Oil & Refining Company to retain the purchase price without any obligation to pay interest on the amount so withheld, until such land shall be furnished or until dispute as to the ownership is settled.

Witnesses: (Witnesses Omitted).

[fol. 33] XV

In the month of December, 1933, the Trustees of Mrs. W. I. Cook Estate, received from Humble Oil & Refining Company a printed letter, dated December 14, 1933, copy of which is attached and marked Exhibit 3.

EXHIBIT 3

Humble Oil & Refining Company

Houston, Texas, December 14, 1933.

Mrs. Cook Estate, re Oil Run Division Order—File Ans. 12-26-33

To all Royalty and Other Owners of Oil from Whom Humble Oil & Refining Company Is Purchasing Crude Oil Within the State of Texas:

You are advised that H. B. No. 154, passed by the Forty-third Legislature, State of Texas, and appearing as Chapter 162 of the General Laws of that session, and which took effect on September 1, 1933, levied taxes on the production

of oil in the State at the rate of 2¢ per barrel so long as the market price thereof is $1.00 per barrel or less, and 2 per cent of the market value when the market value is above $1.00 per barrel, and in addition thereto a regulation pipe line tax of 1/10th of one cent per barrel.

You are further advised that under the law it is made the duty of the purchaser of the oil to collect or deduct said taxes from the proceeds of the oil purchased and remit the amount so deducted to the Treasurer of the State of Texas at Austin.

You are further advised that the law referred to provides that all oil owners, whether owners of royalty or working interests, shall bear this tax, each to pay such part thereof as his interest in the production bears to the entire production, subdivision (6), Sec. 2 of House Bill 154 reading as follows:

[fol. 34] "The tax herein levied shall be borne ratably by all interested parties, including royalty interests; and producers and/or purchasers of oil are hereby authorized and required to withhold from any payments due interested parties, the proportionate tax due."

In compliance with the law Humble Oil & Refining Company has deducted and paid to State Treasurer your proportion of said taxes for the months of September, 1933 and October, 1933, and will each month hereafter deduct a sufficient amount from the proceeds of the oil so purchased to cover each owner's proper proportion of said taxes, and will pay same to the State Treasurer as required by said law.

The enclosed check represents the remainder of the proceeds of your oil purchased during the month of November, 1933, after your part of the tax had been deducted, and paid to State Treasurer, as shown by the accompanying statement. Your attention is called to the fact that the tax imposed by said law shall be paid on the actual oil produced without any tank table deductions and this information is given you to aid you in understanding this statement.

Hereafter similar statements showing the deduction for taxes will be sent you monthly with our checks covering payment for other runs.

Yours very truly, Humble Oil & Refining Company,
James Anderson, Vice President.

XVI

That neither Mrs. W. I. Cook, during her lifetime, nor the executor or Trustees of her estate; have ever been producers, managers or operators of the oil property upon the Cook Ranch, but at all times since the discovery well was brought in in 1926, Roeser & Pendleton, Inc., the lessee, and its assigns, have been the exclusive producers, managers and operators of said property.

That at all times since the discovery well was brought in in February, 1926, Roeser & Pendleton, Inc., lessees, and its [fol. 35] assigns, have had the exclusive right to enter upon the Cook Ranch and explore, manage, develop and operate the same for oil and gas, and to produce and save oil therefrom, being accountable to Mrs. Cook and to the executors and trustees of her estate, for her and their part of the royalty oil and gas provided for in the leases hereinbefore mentioned, copy of one of which is attached hereto and marked Exhibit I.

That at no time since the discovery well was brought in on the Cook Ranch in February, 1926, has either Mrs. Cook or her executors or Trustees ever been engaged in the occupation or business of producing oil from the Cook Ranch or elsewhere, but on the contrary, have merely received from the purchaser, the purchase price for their part of the royalty oil produced from said Cook Ranch by Roeser & Pendleton, Inc., lessee, and its assigns.

XVII

That since September 1, 1933, there has currently been deducted by Humble Oil & Refining Company from the market price of the royalty oil owned by the Trustees of Mrs. W. I. Cook Estate, 2% has been paid over by Humble Oil & Refining Company to the State Comptroller of the State of Texas, with notice that the payment of same has been protested by the Trustees of the Cook Estate, giving as the grounds or bases for such protest, the grounds set forth in plaintiffs petition—that the State law levying such tax is unconstitutional; and at no time have the Trustees of the Cook Estate ever personally paid said 2% tax, nor did they have any control over the Humble Oil & Refining Company's paying said 2% of the market value of their royalty oil to the State Comptroller; nor do they have any control over the character or wording of the protest made by the

Humble Oil & Refining Company to the State Comptroller accompanying each such 2% payment. And in this connection, the Trustees of the Cook Estate have no control over [fol. 36] any other person charged with the duty and obligation of deducting and paying 2% of the value of the Trustees' royalty oil, with respect to making such deduction and payment, and the character of protest given in connection with each such payment.

XVIII

That the approximate one-half royalty oil interest owned by Mrs. W. I. Cook Estate was duly assessed for taxation for State, County, School and Road District purposes by the State and County Tax Assessor of Shackelford County, and by the Tax Collector of the Albany Independent School District, and State, County, School and Road District taxes have been duly paid on said royalty interest each year since Mrs. Cook's death on February 22, 1932, and that during the lifetime of Mrs. W. I. Cook, her said oil royalty interest was duly assessed for State, County, School and Road District purposes by the taxing authorities of Shackelford County, Texas, and she duly paid the taxes assessed against same.

XIX

The correspondence attached hereto, marked Exhibits 4 to 10 inclusive, passed between the Humble Oil & Refining Company and plaintiffs.

* * * * * * *

EXHIBIT 6

Mrs. W. I. Cook Estate: re Division Order

File—Your File—re Gross Production Tax

January 12, 1934.

Attention Mr. J. Q. Weatherly

Humble Oil & Refining Company, Houston, Texas.

DEAR SIRS:

Your letter of January 8th received, acknowledging my letter of December 26th concerning payment to State of

Texas of gross production tax thought to be due by Mrs. [fol. 37] Cook's estate under provisions of House Bill No. 154.

You have misconstrued my letter of December 26th. I did not intend to make request that you make payment of tax, so far as Mrs. Cook's estate is concerned under protest, but that you withhold the payment of the tax, or else any payment that you might make would be at your risk. As stated in your letter, the request was intended to become effective as of December oil run payment.

As stated in my letter of December 26th, I understand the constitutionality of House Bill 154 is now involved in a pending suit brought by royalty owners, and should the tax, as to royalty owners be held invalid, then any payments made by you, not deducted from Mrs. Cook's royalty oil, would be without justification. Until the validity of such law is therefore determined, you should either hold back the tax and not make payment to the state, or else make the payment at your risk.

Very truly yours, —— ——, Independent Executor,
Mrs. W. I. Cook's Estate.

EXHIBIT 7

Humble Oil & Refining Company

Legal Department

Houston, Texas, January 15, 1934.

Re Gross Production Tax, Mrs. W. I. Cook's Estate

Mrs. George Thompson, Jr., Independent Executor, Mrs. W. I. Cook's Estate, Fort Worth, Texas.

DEAR SIR:

I have your letter of January 12th, 1934, demanding that we withhold payment of the tax due the State on the royalty interest of the Estate of Mrs. W. I. Cook.

[fol. 38] You, of course, understand that we cannot do this. The law places upon us, as a producer of the oil, the obligation of deducting and paying to the State the tax on

the royalty as imposed by the act. This is the first demand and request which we have ever had to refrain from making the deduction. All others have permitted us to go ahead and make the payment in full to the State under protest. We will be glad to take that action for you. If this is not agreeable to you, I presume that it is a matter which will have to be taken up with the management as to whether or not, under the circumstances, we should make delivery to you in kind of your part of the oil.

With reference to this, please advise at your earliest convenience.

Yours very truly, Jno. Q. Weatherly.

jqw:jd.

XX

Prior to September of 1933, no part of the gross production tax (payable under the gross production tax laws of Texas, in force prior to the effective date of House Bill No. 154 enacted by the 43rd Legislature at its regular session) was charged to or paid directly or indirectly, or borne directly or indirectly, by Mrs. M. M. Cook estate, or the Mrs. M. M. Cook Memorial Trust. On the contrary, the amounts set forth in paragraph XIV, hereof, as having been paid for royalty oil from the Cook Ranch were paid by the purchaser of the oil, to the said Mrs. M. M. Cook, her Estate and Memorial Trust, without any deduction whatever directly or indirectly on account of the gross production tax payable under the Texas Law.

The entire gross production tax levied under laws in force in Texas prior to September, 1933, was payable by the producer of oil on said Cook Ranch upon the full 100 per cent production of oil therefrom.

[fol. 39] It was the universal custom, practice and construction, of the former gross production tax laws of Texas, (in force prior to September, 1933) not to charge any part of the gross production tax levied thereby against the interest of the oil royalty owner, but the same was charged against and collected from the producer, owning, controlling, managing and operating oil wells in Texas, based upon 100 per cent of the production therefrom and a producer

was never construed by the officers of the State collecting said tax, as including a royalty owned.

* * * * * * *

Wm. McCraw, Attorney General; Hubert Faulk, Asst. Atty. General, Attorneys for Defendants.
William R. Watkins, Attorney for Plaintiffs.

[File endorsement omitted.]

[fol. 40] IN DISTRICT COURT OF TRAVIS COUNTY

54,822

TRUSTEES OF MRS. M. M. (W. I.) COOK ESTATE

vs.

GEORGE H. SHEPPARD, as Comptroller of the State of Texas, et al.

JUDGMENT—Feb. 23, 1935; Filed Feb. 28, 1935

On the 4th day of February, 1935, the above entitled and numbered cause came on to be heard upon the pleadings and the agreed statement of facts filed herein by the parties, and the Court having heard and considered the same, is of the opinion that the general demurrer of the defendants to the plaintiff's petition ought to be sustained because:

(1) The plaintiff's have an adequate remedy at law, and

(2) The law assailed is constitutional;

It is, therefore, on this the 23rd day of February, 1933, ordered, adjudged and decreed by the Court that the defendants' general demurrer to the plaintiff's petition be, and the same is hereby sustained, and the plaintiffs declining to amend, the cause is hereby dismissed.

It is further ordered by the Court that all costs incurred herein be, and they are hereby assessed against the plaintiffs.

To which action and ruling of the Court the plaintiffs excepted and at the same time in open Court gave notice

of appeal to the Court of Civil Appeals for the Third Supreme Judicial District of Texas, at Austin, Texas.

C. A. Wheeler, Judge 53rd Judicial District Court.

[File endorsement omitted.]

[fol. 41] IN COURT OF CIVIL APPEALS OF TEXAS

ASSIGNMENTS OF ERROR FROM APPELLANTS' BRIEF

I

The court erred in sustaining defendants' demurrer to plaintiffs' petition.

II

The court erred in holding House Bill 154, Acts 1933, did not violate the obligation of contract clause of the State Constitution.

III

The court erred in holding House Bill 154, Acts 1933, did not violate the obligation of contract clause of the Federal Constitution.

IV

The court erred in holding House Bill 154, Acts 1933, did not violate the due process clause of the State Constitution.

V

The court erred in holding House Bill 154, Acts 1933, did not violate the due process clause of the 14th amendment to the Federal Constitution.

VI

The court erred in holding that House Bill 154, Acts, 1933, was not violative of Article 3, Section 35, of the Texas Constitution.

VII

The court erred in holding that the challenged law does not violate the equal protection clauses of the State and Federal Constitutions.

VIII

The Court erred in holding that House Bill 11, chapter 214, Acts of the 43rd Legislature 1933, provides a plain, speedy and adequate remedy at law.

[fol. 42]

IX

The court erred in refusing to give judgment in favor of the plaintiffs, regardless of their right to permanently enjoin enforcement of House Bill 154, for the amount of royalty oil held in suspense by the defendants.

X

The court erred in holding the law in question did not impose a property tax on plaintiff's royalty in violation of the property tax provisions of the Texas Constitution.

[fol. 43] In Court of Civil Appeals of Texas

No. 8321

Trustees of Mrs. M. M. (W. I.) Cook Estate

vs.

George H. Sheppard, as State Comptroller of the State of Texas

Appeal from District Court of Travis County

Opinion by Associate Justice Blair

Judgment—Nov. 13, 1935

This cause came on to be heard on the transcript of the record and same being inspected, because it is the opinion of the Court that there was no error in the judgment—It is, therefore, considered, adjudged and ordered that the judgment of the trial court be, and the same is, hereby in all things affirmed. That the appellants, Joseph H. Barwise and Geo. Thompson, Jr., as Trustees of the Estate of Mrs. M. M. (W. I.) Cook, Deceased, principals and Employers Liability Assurance Corporation, Limited, surety, pay all costs in this behalf expended, and this decision be certified below for observance.

[fol. 44] In Court of Civil Appeals of Texas

Assignments of Error in Motion for Rehearing—Filed Nov. 27, 1935

I

The court erred in holding the defendants' demurrer to plaintiffs' petition was properly sustained.

II

The court erred in holding that House Bill 154, Acts of 1933, as amended, does not violate the obligation of contract clause of the State Constitution.

III

The court erred in holding House Bill 154, Acts of 1933, as amended, does not violate the obligation of contract clause of the Federal Constitution.

IV

The court erred in holding House Bill 154, Acts of 1933, as amended, does not violate the due process clause of the State Constitution.

V

The court erred in holding House Bill 154, Acts of 1933, as amended, does not violate the due process clause of the Fourteenth Amendment of the Federal Constitution.

VI

The court erred in holding that House Bill 154, Acts 1933, as amended, was not violative of Article 3, Section 35, of the Texas Constitution.

VII

The court erred in holding that House Bill 154, Acts 1933, as amended, does not violate the equal protection clauses of the State and Federal Constitutions.

VIII

The court erred in impliedly holding that plaintiffs had no right to sue to enjoin the enforcement of House Bill 154, Acts of 1933.

[fol. 45]

IX

The court erred in holding that the plaintiffs are not entitled to judgment against the defendants for the amount held in suspense which has been deducted and withheld from plaintiffs' oil royalty and turned over to the defendants.

X

The court erred in holding that House Bill 154, Acts of 1933, as amended, does not impose a property tax on plaintiffs' royalty in violation of the provision of the Texas Constitution, requiring taxation to be equal and uniform, limiting the amount thereof to 35¢ on the $100.00 valuation, and the provision requiring the levy, assessment and collection of taxes in the County where the property is situated.

XI

The court erred in holding that the Legislature had authority to declare that plaintiffs, royalty owners, are engaged in the business of producing oil, and are therefore subject to and may therefore be required to pay a gross production tax on their royalty, the facts admitted by the demurrer and agreed to in the stipulation of facts filed herein, being that plaintiffs are not in anywise engaged as producers of oil.

XII

The court erred in holding that the obligations of plaintiffs' contract with their lessee that said lessee should "deliver to the credit of the lessor, free of cost, in the pipe line to which it may connect its wells the equal one-eighth (⅛th) part of all oil produced and saved from the leased premises," was not unlawfully impaired in violation of State and Federal Constitutions, by requiring their lessee to withhold or direct the purchaser to withhold 2% of the value of plaintiffs' oil.

[fol. 46]

XIII

The court erred in holding that plaintiffs' contract with the purchaser of their royalty oil was not unlawfully impaired by the requirement that said purchaser withhold from the plaintiffs 2¢ on the dollar, or 2% thereof, to be paid over to the defendants.

XIV

The court erred in holding that the Legislature had Constitutional authority, contrary to the provisions of plaintiffs' lease to require the plaintiffs to bear, or pay any part of a tax assessed as an excise or occupation tax on the privilege of engaging in the business of producing oil where payment of such tax is required to be made, deducted, or withheld by plaintiffs' lessee and purchaser of their oil.

XV

The court erred in holding that the nature of lessors rights under an oil lease were such as to justify the holding that the lessor was engaged in a business or occupation, and thereby subject to the tax in question.

[fol. 47] IN COURT OF CIVIL APPEALS OF TEXAS

[Title omitted]

ORDER OVERRULING MOTION FOR REHEARING—December 18, 1935

Appellant's motion for rehearing. Motion is submitted and overruled.

[fol. 48] IN SUPREME COURT OF TEXAS

TRUSTEES OF MRS. M. M. (W. I.) COOK ESTATE, Plaintiffs in Error,

vs.

GEORGE H. SHEPPARD, as Comptroller of the State of Texas, et al., Defendants in Error

ASSIGNMENTS OF ERROR IN PETITION FOR WRIT OF ERROR—Filed January 20, 1936

I

The Court of Civil Appeals erred in holding the Legislature and defendants could, consistently with the due process clauses of the State and Federal Constitutions, and to ac-

complish the objects of the law in question, say plaintiffs are engaged in the business of producing oil and tax them as for engaging in such business, when they are not in fact engaged therein. (Grounds I, IV, VIII, IX, XI, XV, Plaintiffs' Motion for Rehearing Court of Civil Appeals.)

II

The Court of Civil Appeals erred in holding that House Bill 154, Acts of 1933, as amended, does not impose a property tax on plaintiffs' royalty in violation of the provisions of the Texas Constitution requiring taxation to be equal and uniform, limiting the amount thereof to 35¢ on the $100.00 valuation, and the provision requiring the levy, assessment and collection of taxes in the County where the property is situated. (Grounds I, VIII, IX, X, Plaintiffs' Motion for Rehearing Court of Civil Appeals.)

III

Plaintiffs' leases having vested in the lessee the exclusive right to produce oil, and obligated it to deliver the royalty oil to the lessor's credit in the pipeline free of cost, the Legislature and defendants cannot, consistently with the [fol. 49] obligation of contract clauses of the State and Federal Constitutions, authorize or require the lessee to deliver the royalty oil burdened with a tax on the privilege of engaging in the business of producing it, thereby relieving the lessee of a portion of the cost of production, making the royalty interest less valuable and the method of enforcing the lease entirely different than when the lease was made, and the Court of Civil Appeals erred in holding the contrary. (Grounds I, II, III, VIII, IX, XII, XIV, Plaintiffs' Motion for Rehearing Court of Civil Appeals.)

IV

The Court of Civil Appeals erred in holding that plaintiffs' contract with the purchaser of their royalty oil was not unlawfully impaired by the requirement that said purchaser withhold from the plaintiffs 2¢ on the dollar, or 2% thereof, and pay same to the defendants. (Grounds I, XIII, Plaintiffs' Motion for Rehearing Court of Civil Appeals.)

V

The Court of Civil Appeals erred in holding that House Bill 154, Acts 1933, as amended, was not violative of Article 3, Section 35, of the Texas Constitution. (Grounds I, VI, VIII, IX, Plaintiffs' Motion for Rehearing Court of Civil Appeals.)

VI

The Court of Civil Appeals erred in holding that House Bill 154, Acts 1933, as amended, does not violate the equal protection clauses of the State and Federal Constitutions. (Ground VII Plaintiffs' Motion for Rehearing Court of Civil Appeals.)

VII

The Court of Civil Appeals erred in impliedly holding that plaintiffs had no right to sue to enjoin the enforcement of House Bill 154, Acts of 1933. (Grounds I and VIII Plaintiffs' Motion for Rehearing Court of Civil Appeals.)

[fol. 50] IN SUPREME COURT OF TEXAS

[Title omitted]

ORDER DENYING WRIT OF ERROR—February 5, 1936

This day came on to be heard the application of plaintiff in error for a writ of error to the Court of Civil Appeals for the Third District, and the same having been duly considered, it is ordered that the application be refused; that applicants, Trustees of Mrs. M. M. (W. I.) Cook Estate, and surety, Employers Liability Assurance Corporation, Limited, pay all costs incurred herein.

[fol. 51] IN SUPREME COURT OF TEXAS

[Title omitted]

MOTION FOR REHEARING—Filed February 14, 1936

Plaintiffs in error respectfully pray a rehearing on their petition for writ of error which was denied on February 5, 1936, on the following grounds:

I

The Court of Civil Appeals, and this court by refusing the writ of error, erred in holding the Legislature and defendants could, consistently with the due process clause of the Federal Constitution, arbitrarily provide in the law in question that plaintiffs are engaged in the business of producing oil, when they are not in fact so engaged, in order to pay upon them a tax for which they could not be held liable unless they were so engaged.

II

Plaintiffs antecedent leases having obligated the lessee to deliver plaintiffs' royalty oil to their credit in the pipeline free of cost, the Court of Civil Appeals and this court by refusing the writ of error, erred in holding that the obligation of said leases was not impaired in violation of the obligation of contract clause of the Federal Constitution, by the tax law in question, which authorizes and requires the deduction of two per cent of the proceeds of plaintiffs' oil [fol. 52] and the addition of a like amount to the proceeds of lessee's oil, which relieves the lessee of a part of the cost of producing the oil, makes the plaintiff's royalty interest less valuable, and the method of enforcing the lease entirely different than when it was made.

III

The Court of Civil Appeals, and this Court in refusing the writ of error, erred in holding that the provision of the law in question which requires the purchaser of the oil to withhold two percent of the contract price thereof, does not impair the obligation of said sale contract in violation of the obligation of contract clause of the Federal Constitution.

IV

The Court of Civil Appeals, and this Court in refusing the writ of error, erred in holding that the law in question does not violate the equal protection clause of the Federal Constitution when it is interpreted to mean that royalty oil belonging to the State is exempt from the tax in question although such royalty oil is produced under the same circumstances as other royalty oil.

It is admitted plaintiffs are not producers of oil. The Legislature has arbitrarily declared they are producers in order to impose on them part of a tax for which they could not otherwise be held liable. The Legislature has no authority to ignore the facts and arbitrarily say plaintiffs are producers when they are not. The attempt to so classify them in order to reach their property, which could not otherwise be taken for the purpose, deprives them of their property without due process of law, in violation of the due process clause of the 14th Amendment to the Federal Constitution.

[fol. 53] Under plaintiffs' lease contract the cost of engaging in the business of producing oil is to be borne by the lessee. A part of such cost is the tax imposed on the lessee for the privilege of engaging in the business. The law in question takes from the lessor two per cent of the income the lessee agreed to pay him under the contract, and adds it to the lessee's income. The law clearly intended this result and intended that the lessee should not be responsible to the lessor for the amount so deducted and added. This clearly impairs the obligation of the lease in violation of the obligation of contract clause in the Federal Constitution. The same is true of the contract for the sale of the oil.

Respectfully submitted, William R. Watkins, Attorney for Plaintiffs in Error.

The Attorney General, Austin, Texas, is Attorney for Defendants in Error.

[File endorsement omitted.]

[fols. 54 & 55] IN SUPREME COURT OF TEXAS

[Title omitted]

ORDER OVERRULING MOTION FOR REHEARING—February 26, 1936

It is ordered by the Court that the motion for rehearing herein be overruled.

[fol. 56] In Court of Civil Appeals of Texas

No. 8159

Group No. 1 Oil Corporation, Appellant,

vs.

Geo. H Sheppard, Comptroller, et al., Appellees

Appeal from District Court, Travis County

Opinion—Filed Nov. 27, 1935

Appellant, Group No. 1 Oil Corporation, sued appellees, Geo. H. Sheppard, State Comptroller, and Charley Lockhart, State Treasurer, for the refund of certain gross production taxes on oil, which appellant paid under written protest to appellees. The taxes were alleged to have been wrongfully demanded and collected as being due under the provisions of House Bill No. 154, Acts 43rd Legislature, as amended and reenacted by House Bill No. 55 of the 1st Called Session of the same Legislature, which Acts will be herein referred to as H. B. 154, or the Act, tne material portions of which read, as follows:

"Section 1. (1) For the purpose of this Act 'producer' shall mean any person or persons, corporation, partnership, individual, trustee, receiver, trust estate or administrator owning, controlling, managing or leasing any oil well or any person who produces in any manner any oil by taking it from the earth or waters in this State."

"Section 2. (1) There is hereby levied an occupation tax on oil produced within this State of two (2) cents per barrel of forty-two (42) standard gallons. * * *"

"(2) The tax hereby levied shall be a liability of the producer of oil and it shall be the duty of such producer to keep accurate records of all oil produced, making monthly reports under oath as hereinafter provided."

"(3) The purchaser of oil shall pay the tax on all oil purchased and deduct tax so paid from payment due producer or other interest holder, making such payments so deducted to the Comptroller of Public Accounts by legal tender or cashier's check payable to the State Treasury.

"Provided, that if oil produced is not sold during the [fol. 57] month in which produced, then said producer shall pay the tax at the same rate and in the manner as if said oil were sold."

"(6) The tax herein levied shall be borne ratably by all interested parties, including royalty interests; and producers and/or purchasers of oil are hereby authorized and required to withhold from any payments due interested parties, the proportionate tax due."

The refund of three items of taxes was sought by appellant's petition. The sum of $1,326.25 alleged to have been wrongfully demanded and collected by appellees as the gross production tax on the one-eighth royalty interest of the State University in the oil produced from its Reagan County lands by appellant as lessee thereof and as producer of the oil. The taxes were paid either by appellant or by the purchaser of the oil in the manner prescribed by the taxing act. Another item was for the sum of $209, which was also demanded and collected by appellees as the gross production tax on the one-eighth royalty interest of the University in the oil produced from its lands in Reagan County. The third item was for the sum of $242.27, as to which item appellant alleged that in addition to being a producer of oil, it was the owner of and entitled to receive royalties on oil produced in divers and sundry places from privately owned lands; that the producing operations were conducted by other corporations as lessees, and that these lessees, or purchasers from them, had deducted from settlements with appellant for its royalty interests the sum of $242.27, and in turn had remitted that amount to appellees. The legal consequence was that appellant had thereby been forced to pay and had paid the sum of $242.27 to appellees as the gross production or occupation tax on its royalty interests in the privately owned lands. All of the claims covered payments of taxes for the months of September and December, 1933; and the payments were made under the written protest of appellant as required by H. B. [fol. 58] No. 11, Acts of the 43rd Legislature, which provides that such protested taxes be kept in the "Cash Suspense Book" or account, subject to the suit of the taxpayer for its refund, if unlawfully collected.

The trial court sustained the general demurrer and several special exceptions of appellees to the petition of appellant, and upon its declining to amend dismissed the suit. It was admitted by all parties that because of various constitutional inhibitions the University could not be charged with the gross production tax on its one-eighth royalty interest in the oil produced from its lands; but the trial court construed the Act as imposing the gross production tax due on the one-eighth royalty interest of the University upon appellant, the "producer" of the oil as that term is defined in Section 1 of the Act; and accordingly sustained the general demurrer.

By an excellent brief the Attorney General seeks to sustain the trial court's construction of the Act, and to defend it against the attack that if so construed the Act is unconstitutional. On the other hand, by the excellent briefs of counsel for appellant and of Messrs. Black and Graves, appearing Amici Curiae, representing the Big Lake Oil Company, a lessee of oil producing lands belonging to the University, the contention is made that under a proper construction of the Act, the gross production taxes on oil is levied against the various interest holders, including the producer and royalty owners, in proportion to their respective interests, and as thus construed no greater burden is imposed by the Act on the lessees of University lands than on other lessees of oil producing lands privately owned. That if the Act be construed as imposing the tax upon the lessee producer of oil from University lands on all of the oil produced, and as imposing the tax upon producers of oil from privately owned lands at the same rate per bar- [fol. 59] rel, but on only a fraction or portion of the oil produced, the Act is void as being violative of the equal taxation clauses of Secs. 1 and 2 of Art. 8, and the equal right clause of Sec. 3 of Art. 1 of the Texas Constitution; and of the equal protection and the due process clauses of both the State and the Federal Constitutions; because there is no difference between the situations or occupations of producers of oil from lands owned by the State University and the producers of oil from lands privately owned, which bear any just or reasonable relation to the object or purpose of the Act. And appellant contends that the Legislature cannot under the guise of an occupation tax on the gross production of oil, validly levy the tax against the

owners of royalty interests in the oil produced within this State, for the reason that, with respect to such royalty ownership, they are neither engaged in an occupation nor doing business as contemplated by Art. 8 of the State Constitution.

We construe the Act to levy the tax against the various interest holders in the oil produced, including the producer and royalty owners other than the University, in proportion to their respective interests; that under this construction of the Act no greater burden is imposed on lessees of the University lands than on other lessees of privately owned lands under similar leases for the production of oil; and that as thus construed the Act is valid and constitutional. We also hold that for the purpose of levying a gross production or occupation tax on oil, the Legislature may validly declare the owners of royalty interests in the oil produced to be engaged in the occupation or business of producing oil.

When construed together Subsections 2 and 6 of Section 2 clearly impose the tax "ratably" against "all interested [fol. 60] parties, including royalty interests," and make the producer primarily liable for the payment of the tax. The language that "the tax herein levied shall be borne ratably by all interested parties, including royalty interests," is clear and means that the tax is levied ratably or in proportion to the interest each party has in the oil produced. The language of Subsection 3 of Section 2, that "the producers and/or purchasers of oil are hereby authorized and required to withhold from any payments due interested parties, the proportionate tax due," is also clear and means that a portion of the tax is due from each interested party. If the tax had been levied against the purchaser only, different language would have been employed by the Legislature. There was no reason for providing that the tax be paid ratably or proportionately by all interested parties, if the Legislature had intended to levy the tax against the producer only. The Act clearly designates the parties against whom the tax is levied, the amount each is to pay, and other incidences of the tax.

The provisions that "the tax levied shall be a liability of the producer" does not mean that the tax is levied only against the producer. This provision must be construed together with the other provisions of the Act which declare that the tax is levied against all interested parties ratably

or in proportion to their respective interests in the oil produced.

Nor is the provision that the tax be paid ratably by all interested parties in any manner affected by the provision for the payment of the tax by the producer or purchaser. The provision for a single payment, either by the producer or purchaser, is solely in the interest of the convenient and effective administration of the taxing act. An analogous question was decided in the case of Byrne v. Fulton Oil Co., 278 Pac. 514, 518, wherein the court say:

[fol. 61] "The method of making the operator and the royalty holder jointly liable for the tax and authorizing the operator to withhold from the proceeds of the royalty interest the amount of any tax paid by him, was intended as a certain and expeditious method of collecting taxes on such property, and preventing the possibility of any of it escaping taxation. It was designed to authorize the collection of the tax at the source of the product, in order to avoid the necessity of seeking out each royalty holder for the purpose of effecting collection."

The legislative intent to levy the tax ratably against all interested parties in the oil produced is also clearly evidenced by the language that "the purchaser of oil shall pay the tax on all oil purchased and deduct tax so paid from payment due producer or interest holder," and "withhold from any payments due interested parties, the proportionate tax due." These provisions do not levy the tax against the purchaser. He is merely made the agent of the State to collect from the producer or other interest holders the total amount of the tax due; and he is authorized to charge their respective accounts with "the proportionate tax due." That is, the purchaser withholds from the producer only as an interest holder and only to the extent of his interest. Likewise the purchaser withholds from other royalty or interest holders the amount of the tax due on their royalty or other interests. The Act, therefore, designates the parties against whom the tax is levied. The amount of the tax due by each is also defined or measured by the extent of interest in the oil produced, or the amount paid because it was produced. This language and these provisions must

be given practical effect and application in the interpretation or construction of the Act; and since the purchaser is given the right in making payments due the producer or other interest holders, to withhold the sum of money equal to "the proportionate tax due," it must be held that the Act imposed the tax on the producers and other interest holders ratably or in proportion to their respective inter- [fol. 62] ests in the oil produced. The language of the Act is plain, unambiguous and susceptible of no other reasonable interpretation or construction.

This construction is not only supported by the clear and unambiguous language of the Act, but is required to save it from the vice of unconstitutionality. It is clear that if the producer is liable for the entire tax on oil produced on University lands and the producer of oil from privately owned lands is liable for the tax on only 7/8 of the oil produced, a greater burden, or an unequal taxation burden will be placed upon the producer of oil from University lands. Since, however, we hold that the practical effect of the Act is to impose the tax on the producer and other interest or royalty holders ratably or in proportion to their respective interests; and since the Act placed the collection of the tax in the hands of the producer to such an extent that he can never be required to pay more than his proportionate part of the tax, we do not need to discuss at length the constitutionality of the Act as against the attacks made by appellant.

Suffice it to say that under our above construction of the Act no greater tax burden has been placed or imposed by it on lessees of University lands than on lessees of privately owned lands being operated for oil under the same or similar lease contracts. The lessee or producer under a lease from the State or University receives seven-eighths of the oil produced, or its value, as consideration for the development of the lease, and the State or University owns or receives a "royalty interest" of one-eighth, or a "sum of money equal to a royalty of one-eighth of the value of the gross production of petroleum." Section 7 (2) General Laws, 1917, Chap. 83, pp. 158, 160. This "royalty" is payable in money, but is secured by a statutory lien on the oil and improvements on the property. The courts (Theisen v. Robison, 117 Tex. 489) interpret the Act of 1917 as conveying to the lessee title to all the oil and gas in place; and

[fol. 63] appellees therefore contend that lessee must pay all the tax imposed by the Act involved in this suit, without any deduction on account of the University's royalty interest. Lessee may not be the producer, and may receive an interest in the oil from the producer. It is also a matter of common knowledge that many leases on privately owned lands provide that the one-eighth "royalty" is to be paid in money received from the sale of the oil produced. Others provide for the delivery of one-eighth of the oil produced as royalty, and in which leases the lessee acquires title to only seven-eighths of the oil, the lessor reserving title to the remaining one-eighth. So, it is manifest that the same distinction which appellees urge with respect to the character of title acquired under a state lease and some private leases can also be made as between private leases. Certainly the same distinction and discrimination would exist in applying the taxing act to operations under private leases having similar royalty provisions to State or University leases. But whatever the character of the lease, or whether a State or a private lease, there is always reserved a royalty interest of one-eighth of the oil or a royalty interest equal to one-eighth of the value of the oil produced, sold or unsold, and manifestly this is the "royalty interest" within the contemplation of the taxing act in suit, and against the owner of which the tax was levied. And manifestly the lessee under a State or University land lease assumes substantially the same obligations, expressed and implied, as are assumed by lessees of privately owned lands which have for their purpose the diligent and proper development of the lands for oil, to the end that the amount of the royalty which may be due either in oil or its equivalent may be as large as possible. It may be further observed here that the distinction urged by appellees has not been looked upon with favor by the courts, but all royalty [fol. 64] interests have been placed upon a level by them. At least that is the present tendency of court decisions. Sheffield v. Hogg, 77 S. W. (2d), 1021; Ehlinger v. Clark, 117 Tex., 557; State v. Armson, 207 N. W., 727, 730.

It is also manifest that the tax is not dependent upon the character of title under which the producer produces the oil. Nor is the tax levied on the oil in place. The tax is levied on the business or occupation of producing the oil. The lessees or producers engaged in producing oil on Uni-

versity lands are engaged in the taxed occupation in the same manner as are those who produce oil from privately owned lands, and it would seem that the source or character of title would have nothing to do with the nature of the occupation or business, and such matters are irrelevant with respect to the purposes of the taxing act. Quaker City Cab Co. v. Pennsylvania, 277 U. S. 389, 400; Louisville Gas & Electric Co. v. Coleman, 277 U. S. 32, 37; Southern Railway Co. v. Greene, 216 U. S. 400, 417.

Nor does the fact that the State or University is not liable for the tax levied against the royalty interest enlarge or change the tax liability of the lessee or producer of oil on University lands. This is because, as herein above pointed out, the levy of the tax is made against or limited to the interest of the lessee or producer. The taxing act clearly provided that the royalty interest would be taxed against the owner or holder of the royalty interest. And the fact that the royalty interest belongs to the University, and the fact that the tax cannot be levied against it, does no increase appellant's liability for the tax, but appellant is only required to pay the proportion of the tax levied against it by the taxing act. In the case of Davis v. Wallace, 257 U. S., 478, it is held, as follows:

[fol. 65] "Where an excepting provision in a statute is found unconstitutional, courts very generally hold that this does not work an enlargement of the scope or operation of other provisions with which that provision was enacted and which it was intended to qualify or restrain. The reasoning on which the decisions proceed is illustrated in State ex rel McNeal v. Dombaugh, 20 Ohio St., 167, 174. In dealing with a contention that a statute containing an unconstitutional proviso should be construed as if the remainder stood alone, the court there said: 'This would be to mutilate the section and garble its meaning. The legislative intention must not be confounded with their power to carry that intention into effect. To refuse to give force and vitality to a provision of law is one thing, and to refuse to read it is a very different thing. It is by a mere figure of speech that we say an unconstitutional provision of a statute is "stricken out." For all the purposes of construction it is to be regarded as part of the act. The meaning of the legislature must be gathered from all they have said, as

well from that which is ineffectual for want of power, as from that which is authorized by law.' ''

The Act merely levied the tax against royalty and other interests ratably, and we do not regard the tax as having been levied against the State or University royalty interest, because the Legislature will be presumed to know that the tax could not be lawfully levied against the State or University. Since, however, appellant's tax liability was limited to its interest in the oil produced, and since by subtracting the tax on the royalty interest of the University, because the tax on such interest if levied by the Act was void, appellant's liability was not increased nor enlarged because the attempt to tax the University's royalty interest was void. See also Tex-Louisiana Power Co. v. Farmersville, 67 S. W. (2d), 235.

We are also clear in the view that for the purpose of levying the gross production tax on the occupation or business of producing oil, the Legislature may validly declare the owners of royalty or other interests in the oil produced to be engaged in the occupation or business of producing oil. The ordinary form of oil lease has a dual character or purpose: 1) the conveyance of an estate in the land for development purposes; and 2) the future development and operation of the lease for oil in accordance with the terms, [fol. 66] express and implied, of the contract for the mutual benefit of the parties, their respective benefit being measured by the extent of their interests in the oil produced, or its value. The law is settled that the primary objective or purpose of the oil lease is the production of oil for the mutual profit of the parties. The consideration moving to the lessor is an interest in the oil or its value in money. Thus he has a direct interest in the success of the business. As the holder of the royalty interest the lessor or royalty owner is not only entitled to share in the gross production of the oil, but may under the terms of the lease, expressed or implied, require proper, prudent and diligent management and development of the business, and has reserved and is entitled to both legal and equitable remedies necessary to enforce the obligations of the lease, and under some circumstances may forfeit the lease for non-development. Texas Co. v. Davis, 113 Tex. 321; Robinson v. Jacobs, 113

Tex., 231; Thomason v. Ham, 113 Tex., 239; Munsey v. Marnett Oil & Gas Co., 113 Tex. 212.

The tax of 2¢ per barrel on oil produced is a gross production or gross receipts tax, the amount of the tax being measured by the gross activity of the business, and is under the authorities an occupation tax. G. H. & S. A. Ry. v. Davison, 93 S. W. 436; G. H. & S. A. Ry. Co. v. State, 210 U. S. 217; Producers Oil Co. v. Stephens, 99 S. W. 157; Kansas City Life Ins. Co. v. Love, 101 Tex., 531. And since the taxing act in suit contemplated a tax on gross production of oil, the amount of the levy being measured or determined by the gross receipts of the oil or business, we conclude that the Legislature may reasonably impose the tax burden on those entitled to share in the gross receipts or profits of the oil enterprise, particularly so since under the lease contracts royalty owners may enforce its express and implied covenants, looking to the proper and diligent development and [fol. 67] management of the business, to the end that their share in the receipts will increase and produce a greater royalty interest in the business.

In accordance with our above conclusions, we affirm the judgment of the trial court as to the item of $242.27, paid as the gross production or occupation tax due on the royalty interest of appellant from privately owned lands; but the judgment otherwise dismissing the suit is reversed and the cause remanded for trial of the facts alleged in the petition.

M. B. Blair, Associate Justice.

Affirmed in Part and in Part Reversed and Remanded.
Filed Nov. 27, 1935.

[File endorsement omitted.]

[fol. 68] IN COURT OF CIVIL APPEALS OF TEXAS

No. 8321

TRUSTEES OF MRS. M. M. (W. I.) COOK EST., Appellants,

vs.

GEO. H. SHEPPARD, as Comptroller of the State of Texas, et al., Appellees

Appeal from District Court, Travis County

OPINION—Filed Nov. 13, 1935

This case is companion to and in most respects is controlled by our decision in the case of Group No. 1 Oil Corporation v. Sheppard, Comptroller et al., — S. W. (2d), —, this day decided. Appellants herein sued George H. Sheppard, State Comptroller, and Charley Lockhart, State Treasurer, for the refund of certain gross production taxes on oil, which they paid under written protest to appellees, aggregating $907.22. The taxes were demanded and collected as being due under H. B. 154, the material portions of which were quoted in the opinion in the companion case; and as being the gross production or occupation tax levied against the one-eighth royalty interests of appellants under their oil leases covering the Cook Ranch in Shackelford County. The leases are the usual form of oil leases, and provide that lessee shall "deliver to the credit of the lessor, free of cost in the pipeline to which it may connect its wells, the equal one-eighth part of all oil produced and saved from the leased premises."

We construe the taxing act in the companion case to levy the tax against the various interest holders in the oil produced or its value, including the producer and royalty owners other than the State University, ratably or in proportion to their respective interests. This construction of the act in the companion case disposes of most of the constitutional defenses interposed by appellants in this case, and [fol. 69] only one additional constitutional question will be discussed.

Appellants contend that the taxing act in suit is violative of the obligation of contract clauses of both the State

and Federal Constitutions, for the reasons: 1) that it impairs the antecedent obligations of appellants' lessee to deliver them the equal one-eighth part of the oil produced, free of costs, the taxing act in force at the time of the execution of the contract having required the lessee to pay the entire gross production tax on the oil; and 2) that the present taxing act requires the producer with whom appellants had a contract prior to the enactment of such taxing act to pay them the regular posted price for the royalty oil, to deduct from the royalty interests due the proportionate amount of the gross production tax, and remit the same to the State officials named. Manifestly this taxing act does not change in any manner the lease contracts between the parties. The tax is not against the oil royalty. It is levied as a gross production tax on the business or occupation of producing oil. The tax belongs to the State, and the mere fact that the producer is primarily liable for the payment of the tax, or the fact that the purchaser is required to collect the tax for the State at its source or origin, does not give them any interest in the tax against the royalty interests. They may have benefited by the change of legislative policy of imposing the tax ratably against the respective interest holders in the oil produced; but such legislative tax policy did not impair any obligation of the lease contracts.

In this connection appellants cite several cases in support of the contention that royalty owners under the [fols. 70 & 71] ordinary form of oil and gas leases are not engaged in the business of producing oil. None of these cases is in point. The dicta in the case of Flynn v. State Tax Com., 28 Pac.-(2), 889, is to the contrary. It reads:

"Our minds do not reject the idea that the lessee and the royalty owner, considered as participating in a joint enterprise, are both engaged in the business of producing or severing oil, and that the tax is therefore essentially occupational. Such a view, however, is not indispensable to sustaining the tax. For it may be considered occupational as to the lessee, and another kind of tax to the royalty owner. Unless found as to one or the other, to be a tax upon tangible property it need not be levied ad valorem, and is an excise."

The point involved was left undecided in Byrne v. Fulton Oil Co., 78 Pac. 514, because the statute construed did

not impose the tax on the royalty interest. This case does hold, however, that the levy of a tax on the royalty interest in lieu of a property tax, the tax to be paid by the producer with right to deduct the amount of the tax paid in making settlement with the royalty owner, did not impair the obligation of the lease contract. See also Lake Superior Consolidated Iron Mines v. Lord, 271 U. S. 577. Our view that the Legislature may validly declare the owners of royalty interests in the oil produced to be engaged in the business or occupation of producing oil for the purpose of levying the occupation tax against them is fully expressed in the companion case, with citation of authorities which we construe as sustaining that view. That view need not be reiterated here.

We find no error in the judgment of the trial court holding the tax act to be constitutional and dismissing appellants' suit for a refund of the taxes paid, and it will be affirmed.

M. B. Blair, Associate Justice.

Affirmed.

Filed Nov. 13, 1935.

[File endorsement omitted.]

[fol. 72] In Court of Civil Appeals of Texas

[Title omitted]

Petition for Appeal—Filed March 7, 1936

To said Honorable Court:

The appellants, George Thompson, Jr., and J. H. Barwise, Trustees of the Estate of Mrs. M. M. (W. I.) Cook, deceased, in the above cause respectfully represent:

1. November 13, 1935, this Court affirmed the judgment of the District Court of Travis County, Texas, dismissing plaintiffs' cause, holding in that connection that the Act of the Texas Legislature known as House Bill 154, Acts 1933, did not contravene the due process clause of the Fourteenth Amendment to, and the obligation of contract clause of the Federal Constitution, as claimed by appellants.

2. Appellants duly applied to the Supreme Court of Texas urging reversal of the judgment of this Court and reiterating their claim that said law contravenes said clauses of the Federal Constitution. The Supreme Court refused the petition for writ of error February 5, 1936, and overruled our motion for rehearing February 26, 1936, and has returned the record in the cause to this court which is [fol. 73] therefore the highest court of the State in which a decision may be had.

3. Appellants desire to appeal from the judgment of this Court to the Supreme Court of The United States, and present herewith the requisite Assignment of Errors, Statement as to Jurisdiction, and security for costs on their said appeal.

Wherefore, appellants pray that upon consideration hereof an order be entered allowing them an Appeal herein to the Supreme Court of the United States.

William R. Watkins, Attorney for Appellants.

[File endorsement omitted.]

[fol. 74] In Court of Civil Appeals of Texas

[Title omitted]

Assignment of Errors—Filed March 7, 1936

The appellants assign the following errors in the proceedings and decree of the Court of Civil Appeals, which they will urge upon their appeal to the Supreme Court of the United States:

I

The Court of Civil Appeals erred in holding the Legislature and appellees could, consistently with the due process clause of the Federal Constitution, arbitrarily provide and say in and under the law in question that appellants are engaged in the business of producing oil, when they are not in fact so engaged, in order to lay upon them a tax for which they could not be held liable unless they were so engaged.

II.

Appellants antecedent leases having obligated the lessee to deliver appellants' royalty oil to their credit in the pipeline free of cost, the Court of Civil Appeals erred in holding [fol. 75] that the obligation of said leases was not impaired in violation of the obligation of contract and due process clauses of the Federal Constitution, by the tax law in question, which authorizes and requires the deduction of two percent of the proceeds of appellants' oil and the addition of a like amount to the proceeds of lessee's oil, which relieves the lessee of a part of the cost of producing the oil, makes the appellants' royalty interest less valuable, and the method of enforcing the lease entirely different than when it was made.

III

The Court of Civil Appeals erred in holding that the provision of the law in question which requires the purchaser of the oil to withhold two percent of the contract price thereof, does not impair the obligation of said sales contract in violation of the obligation of contract clause of the Federal Constitution.

IV

The Court of Civil Appeals erred in holding the law in question does not contravene the provisions of the Federal Constitution mentioned in plaintiffs' petition.

V

The Court of Civil Appeals erred in holding appellants were not entitled to recover the taxes exacted, and to enjoin the future taxes assessed under the law in question.

Wherefore, premises considered, appellants pray that upon consideration of their appeal the decree of the Court of Civil Appeals be reversed.

William R. Watkins, Attorney for the Appellants.

[File endorsement omitted.]

[fols. 76-82] In Court of Civil Appeals for the Third Supreme Judicial District of Texas, at Austin

No. 8321

Mrs. M. M. (W. I.) Cook Estate, Trustees, Appellants,

vs.

George H. Sheppard, As Comptroller of the State of Texas, and Charley Lockhart, As State Treasurer of Texas

Order Allowing Appeal—Filed March 7, 1936

On this the 7 day of March, 1936, upon consideration of the appellants' petition for the allowance of an appeal to the Supreme Court of the United States from the final judgment against them herein, the Appellants' assignment of errors and jurisdictional statement, filed as required by Rule 12 of the Supreme Court of the United States, accompanying and being considered in connection with the same; and it appearing that a writ of error has been refused by our Supreme Court herein and the record in the cause returned to this Court where by law it remains,

It is ordered, by the undersigned Chief Justice of the Court of Civil Appeals for the Third Supreme Judicial District that said petition for appeal be, and the same is hereby allowed, upon filing and approval of security for costs in the sum of $500.00.

Jas W McClendon, Chief Justice, Court of Civil Appeals for the Third Supreme Judicial District of Texas.

[File endorsement omitted.]

[fol. 83] Supreme Court of the United States

Appellants' Statement of Points to Be Urged and of Parts of the Record to Be Printed—Filed March 12, 1936

Pursuant to the provisions of Paragraph 9, Rule 13 of the Court, the appellants make the following statement of the points on which they intend to rely, to-wit:

1. It being an admitted fact that appellants are not engaged in the business of producing oil, the Texas Gross Production Tax law of 1933, as Amended, which arbitrarily provides that they are engaged in such business, to lay an otherwise prohibited tax upon them, contravenes the due process clause of the Fourteenth Amendment to the Federal Constitution.

2. Appellants antecedent lease having obligated the lessee to deliver appellants' royalty oil to their credit in the pipe line free of cost, the tax law in question which authorizes and requires the deduction of two per cent of the proceeds of appellants' oil and the addition of a like amount to the proceeds of their lessee's oil, which relieves the lessee of a part of the cost of producing the oil, makes the appellants' royalty interest less valuable, and the method of enforcing the lease entirely different than when it was made, violates the due process clause of the Fourteenth Amendment to, and the obligation of contract clause of the Federal Constitution.

[fol. 84] 3. The law in question violates the obligation of contract clause of the Federal Constitution in requiring the purchaser of their oil who is obligated under an antecedent contract to pay its posted price therefor, to pay only 98% of such price and give their lessee the benefit of the 2% deduction.

Appellants deem the following parts of the record necessary for consideration of the points to be urged and request that same be printed:

1. Petition,
2. Answer,
3. Agreed Statement of Facts,
4. Judgment District Court,
5. Assignments of Error in Court of Civil Appeals,
6. Judgment Court of Civil Appeals,
7. Assignments of Error, Motion for Rehearing C. C. A.,
8. Order Overruling Motion for rehearing,
9. Assignments of Error in Supreme Court on Writ of Error,
10. Order Supreme Court denying Writ of Error,
11. Motion for rehearing Supreme Court,

12. Order Overruling Motion for Rehearing Supreme Court,
13. Opinions Court of Civil Appeals in Group No. 1 Oil Corporation v. Sheppard and in this case,
14. Petition for Appeal,
15. Assignment of Errors,
16. Order Allowing Appeal,
17. This Designation.

William R. Watkins, Attorney for the Appellants.

The appellees acknowledge service of the foregoing designation by the appellants of the points they intend to rely upon and of the parts of the record to be printed. The appellees waive the right to file a further designation as authorized by Rule 13, Paragrah 9.

This the 7 day of March, 1936.

Hubert T. Faulk, Assistant Attorney General for the Appellees.

[fol. 85] [File endorsement omitted.]

Endorsed on cover: File No. 40,378. Texas Court of Civil Appeals, Third Supreme Judicial District. Term No. 824. Joseph H. Barwise and George Thompson, Jr., as Trustees of the Estate of Mrs. M. M. (W. I.) Cook, Deceased, Appellants, vs. George H. Sheppard, as Comptroller of the State of Texas, et al. Filed March 12, 1936. Term No. 824, O. T., 1935.

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1935

No. 824

MRS. M. M. (W. I.) COOK ESTATE, TRUSTEES,
Appellants,

vs.

GEORGE H. SHEPPARD, AS COMPTROLLER OF THE STATE OF TEXAS, AND CHARLEY LOCKHART, AS STATE TREASURER OF TEXAS,
Appellees.

STATEMENT AS TO JURISDICTION.

This suit was instituted by appellants against the State officers named as appellees, to restrain the enforcement of the Texas Gross Production Tax Law of 1933,[1] as applied to royalty oil, and to collect from the State officials the amount of tax already exacted, on the ground that the law, both in terms and as applied to them, violates the obligation of their antecedent oil lease and oil sales contracts and deprives them of their property without due process, in violation of the obligation of contract and due process of law clauses of the State and Federal Constitutions. The law

[1] Its pertinent provisions are set out at the end of this statement.

was incidentally challenged, also, on the ground it violated other provisions of the State Constitution which it is not necessary to now outline.

Long before the enactment in question, appellants, as trustees, owned royalty under leases which granted the lessees the exclusive right to engage in the business of producing oil from the land covered thereby and required the lessees "to deliver to the credit of lessor, *free of cost,* • • • the equal one-eighth part of all oil produced and saved from the leased premises." Appellants had written contracts for the sale of their oil to the Humble Oil & Refining Company, by which the company agreed to pay them the full posted price of the oil, without deduction. Appellants are not and have never been in anywise engaged in the business of producing oil. Appellees admit these facts (R. 18, 30, 34).

At the time the aforesaid contracts were made the Texas law laid a gross production tax of two per cent of the value of all oil produced upon the producer alone (R. 38).

The law in question (H. B. 154, Acts 1933, 43rd Legislature p. 409, ch. 162, as amended Acts 1933, 43rd Legislature First Called Session p. 43, ch. 12, Vernons Annotated Texas Statutes 1925, Supp. Art. 7057-A) levies what is denominated "an occupation tax on oil produced within this State of two cents per barrel • • •. Said tax shall be computed upon the total barrels of oil produced • • • without any deductions." Under other provisions the tax is two per cent on each barrel if the value is in excess of $1.00 per barrel. While it is provided the tax "shall be a liability of the producer of oil and it shall be the duty of such producer to keep accurate records of all oil produced" and make reports to the Comptroller, it is further provided that the tax "*shall be borne ratably by all interested parties, including royalty interests*" and producers and purchasers are required to withhold from payments due interested parties, the proportionate tax due. By amendment made since this suit was

filed royalty owners are included in the definition of the term "producers" as used in the Act.*

The tax for the oil run in one month must be paid by the purchaser to the Comptroller, by the 25th of the month next after it is produced. Elaborate reports are required from the purchaser in connection with purchases of oil.

The Act provides that, "for the ocupation tax, penalties, and interest herein provided for the State shall have a prior and preferred lien on any leasehold interest, ownership of oil rights, or interest, including oil produced."

Since enactment of the law the Comptroller, purporting to act under the same, has required the Humble Company to deduct two cents per barrel from the price due appellants for their royalty oil, and pay it over to the State (R. 20-21). If appellants refuse to acquiesce in this arrangement their oil will be rejected by the purchaser (R. 36-38), and, under regulations of the Comptroller, they must pay the tax direct (R. 18).

We challenged this law in our petition (R. 9-11) in the State District Court on the ground it violated the obligation of contract and due process clauses of the Federal Constitution. We have alleged and maintained throughout:

1. A State cannot by a system of taxation directly impair the obligation of a private contract, *Murray* v. *Charleston*, 96 U. S. 44. The lease contract required the lessee to pay all expenses incident to engaging in the business of producing oil. A primary object of the law is to relieve our lessees of a part of the burden they voluntarily assumed in their leases. The State, under the law in question, requires the appellants to pay one-eighth of a tax imposed for the privilege owned exclusively by their lessee of engaging in the business of producing oil from the leases.

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*This provision of the amendment is set out at the end of this statement.

The purchaser, as agent of the State, deducts this part of the tax from appellants' remittance and sends it to the appellees. The substantial effect of the law is to give the lessee two cents or two percent more per barrel of oil than he is entitled to under the lease and prevent the lessor recovering the same. Such a law clearly impairs the due process and obligation of contract clauses of the Federal Constitution.

2. The law in question seeks to evade the provisions of the Texas Constitution which prohibit taxation of property except it be equal and uniform throughout the State, levied in the county where the property is situated, equalized by the County Commissioners Courts and limited in amount to 35 cents on the $100.00 valuation.[1] The fatal defect in the attempt to evade these constitutional inhibitions lies in the fact that the Legislature cannot, consistently with the due process clause of the Fourteenth Amendment to the Federal Constitution, arbitrarily declare appellants are engaged in the business of producing oil when they are admittedly not so engaged in fact. Occupation taxes or excises may be levied upon proper subjects, but the Legislative power cannot, consistently with due process, be exercised to arbitrarily create the conditions under which the liability shall exist, irrespective of the truth. To define as producers of oil, people who are not producers, in order to levy an otherwise unlawful tax upon them is the grossest sort of confiscation.

The Court of Civil Appeals held:

> "We construe the act to levy the tax against the various interest holders in the oil produced, including the producer and royalty owners,"

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[1]Under the Texas law royalty is real estate and taxable as other property as provided by the Constitution of Texas. *Sheffield* v. *Hogg*, 77 S. W. (2d) (Sup. Ct.) 1021.

"Whatever the character of the lease * * * there is always reserved a royalty interest * * * and manifestly this is the 'royalty interest' within the contemplation of the taxing act in suit, and against the owner of which the tax was levied."

"For the purpose of levying the gross production tax on the occupation or business of producing oil, the Legislature may validly declare the owners of royalty or other interests in the oil produced to be engaged in the occupation or business of producing oil." "The Legislature may reasonably impose the tax burden on those entitled to share in the gross receipts or profits of the oil enterprise * * * since under the lease * * * royalty owners may enforce its * * * covenants * * * to the end that their share of the receipts will increase and produce a greater royalty interest in the business." "The tax is not against the oil royalty. It is levied as a gross production tax on the business or occupation of producing oil." "The mere fact the producer is primarily liable * * * or * * * that the purchaser is required to collect the tax * * * does not give them any interest in the tax against the royalty interests. They (the producers) may have benefitted by the change of Legislative policy of imposing the tax ratably against the respective interest holders in the oil produced; but such Legislative tax policy did not impair any obligation of the lease contracts."

The holding of the Court of Civil Appeals that the lessor's right to enforce the lease "engages" him in the business of producing oil, is notable. We submit that the right to make the lessee produce and deliver the lessor's royalty oil is the very essence of the lessor's property right in the leased land. To tax that right, directly taxes the property itself. *Pollock* v. *Farmers Loan & Trust Company,* 157 U. S. 429, 158 U. S. 601. "It cannot be made an occupation or license tax by calling it so." *Dawson* v. *Kentucky Distilleries,* 255 U. S. 288.

The Court of Civil Appeals for the Third Supreme Judicial District at Austin, decided the case November 13, 1935 (R. 43). The Supreme Court of Texas denied a writ of error February 5, 1936 (R. 50), thereby approving the action of the Court of Civil Appeals. On February 26, 1936, it overruled a motion for rehearing of the application for writ of error, and thereupon returned the record to the Court of Civil Appeals (R. 76). The Court of Civil Appeals is the highest court of the State in which a decision could be had. The appeal to this Court was allowed by the Chief Justice of the Court of Civil Appeals, March 7, 1936.

State Procedure.

Finality of judgment Court of Civil Appeals, Vernons Tex. Civ. Stats., Art. 1857-8.

Jurisdiction Supreme Court on writ of error, Vernons Tex. Civ. Stats. Art. 1728 as amended.

Denial writ of error is approval judgment Court of Civil Appeals, Id. Art. 1728, and refusal to admit case to Supreme Court, Id. Art. 1750.

Jurisdiction This Court.

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General Rule as to appeal from highest State court.
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St. L., S. F. & T. R. Co. v. *Seale*, 229 U. S. 156;
cf. *Bain Peanut Co.* v. *Pinson*, 282 U S. 499, 502;
Id. 34 S. W. (2d) 1090.

Court in which record remains is highest State court.
Hodges v. *Snyder*, 261 U. S. 600;
Rothschild v. *Knight*, 184 U. S. 334;
McDonald v. *Massachusetts*, 180 U. S. 311.

The challenged decision is not sustainable on any ground independent of the Federal questions which were decided adversely to appellants and which control the case. *Lynch* v. *New York*, 293 U. S. 52.

It is respectfully submitted that this Court has jurisdiction to hear the appeal.

Respectfully submitted,

WILLIAM R. WATKINS,
Attorney for Appellants.

APPENDIX.

The Daniel Production and Occupation Tax Law.

(Approved May 22, 1933.)

H. B. No. 154

SEC. 2. (1) There is hereby levied an occupation tax on oil produced within this State of two (2) cents per barrel of forty-two (42) standard gallons. Said tax shall be computed upon the total barrels of oil produced * * *. The occupation tax therein levied on oil shall be two per cent (2%) of the market value of said oil whenever the market value thereof is in excess of one dollar ($1) per barrel. * * *

(2) The tax hereby levied shall be a liability of the producer of oil.

(3) The purchaser of oil shall pay the tax on all oil purchased and deduct tax so paid from payment due producer or other interest holder, making such payments so deducted to the Comptroller of Public Accounts by legal tender or cashier's check payable to the State Treasurer.

Provided, that if oil produced is not sold during the month in which produced, then said producer shall pay the tax at the same rate and in the manner as if said oil were sold.

(6) The tax herein levied shall be borne ratably by all interested parties, including royalty interests; and producers and/or purchasers of oil are hereby authorized and required to withhold from any payments due interested parties the proportionate tax due.

SEC. 6. For the occupation tax, penalties, and interest herein provided for, the State shall have a prior and preferred lien on any leasehold interest, ownership of the oil rights, or interest, including oil produced and oil runs owned by the person owing any tax herein, and in addition thereto such lien shall include equipment, tools, tanks, and

all other implements used on said lease from which oil is produced.

Oil Taxes with Penalties for Evasion.

(Approved May 30, 1935.)

H. B. No. 89

"SEC. 1 (1). For the purpose of this Act 'producer' shall mean any person owning, controlling, managing or leasing any oil well and/or any person who produces in any manner any oil by taking it from the earth or waters in this State, and shall include any person owning any royalty or other interest in any oil or its value, whether produced by him, or by some other person on his behalf, either by lease, contract or otherwise.

"(9). 'Royalty owners' shall mean and include all persons owning any mineral rights under any producing leasehold within this State, other than the working interest, which working interest is that of the person having the management and operation of the well.

"(16). If the oil produced by said producer is not sold during the month in which it is produced, then said producer shall pay the tax at the same rate and in the same manner as if said oil were sold during said month. In such case, however, the working interest operator may pay such tax and deduct it from the interest of the other interest holders."

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Supreme Court of the United States

October Term A. D. 1936

No. 10

JOSEPH H. BARWISE AND GEORGE THOMPSON, JR., as Trustees of the Estate of Mrs. M. M. (W. I.) Cook, Deceased.

Appellants,

vs.

GEORGE H. SHEPPARD, as Comptroller of the State of Texas, Et Al,

Appellees.

Appeal From the Court of Civil Appeals, Third Supreme Judicial District of Texas

(Reported 89 S. W. (2d) 1026)

APPELLANTS' BRIEF

Grounds of Jurisdiction

This appeal, from the final judgment of the highest court of the State of Texas in which a decision herein could be had, involves the validity of a statute of the State of Texas which appellants challenge, both in terms and as applied, as being repugnant to the Constitution of the United States. The decision of the

state court was in favor of its validity. The law in question (H. B. 154, Acts 1933, 43rd Legislature, page 409, Chapter 162, as amended 1933 First Called Session, page 43, Chapter 12 Vernon's Annotated Texas Statutes, 1925, Supp., Art. 7057-A[1]) levies what is denominated "an occupation tax on oil produced within this state." It provides that the tax "shall be borne ratably by all interested parties including royalty interests."

Appellants are not, in fact, producers of oil or engaged in the business or occupation of producing oil. (R. 7, 26-27, 31, infra pp. 11-13). They own royalty under oil leases owned and operated exclusively by their lessee. The two per cent tax has been collected from them, over their protest, since the law was enacted. (R. 17-19). They sued to enjoin collection of the tax and to recover amounts already collected on the grounds, among others, that the law violates the due process clause of the Fourteenth Amendment, and the obligation of contract clause of the Federal Constitution because: (a) While appellants are not engaged in the business or occupation of producing oil they are arbitrarily said to be so engaged and are taxed accordingly, and (b) part of the royalty payable to them under their leases is appropriated for the benefit of their lessee, in violation of lease contracts. (R.1-10).

These grounds were alleged in appellants' petition (R. 7-10) filed in the trial court, but that court held

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1. See Appendix A, infra pp. 32-51.

"the law assailed is constitutional" (R. 35); they were raised by assignments of error in the Court of Civil Appeals, (R. 36) which affirmed the trial court and upheld the constitutionality of the law, as an occupation tax, on the ground the Legislature had the right to declare appellants were engaged in the business of producing oil, because of their "interest in the success of the business" and, that the obligation of the lease was not impaired, (R. 45-57, and see summary of the opinions infra pp. 14-17). The same errors were assigned in the motion for rehearing in the Court of Civil Appeals (R. 38-40) which was denied (R. 40). The same grounds were urged in a petition for writ of error to the Supreme Court of Texas, (R. 40-42) which was refused (R. 42) and appellants' motion for rehearing, in which the same errors were again assigned, was also denied, (R. 42-44). The decision of the Court of Civil Appeals in this case is reported in 89 S. W. (2) 1026. See similar case, *Group No. 1 Oil Corporation v. Sheppard*, 89 S. W. (2) 1021.

The validity of the law under the Federal Constitution was, therefore, properly drawn in question by objections properly taken, *Zucht v. King*, 260 U. S. 174, *Sultan Ry. v. Department of Labor*, 277 U. S. 135, *Sprout v. South Bend*, 277 U. S. 163, *Lee v. Osceola & L. R. R. Imp. Dist.*, 268 U. S. 643, *Fiske v. Kansas*, 274 U. S. 380.

If we correctly interpret the opinion of the Court of Civil Appeals, this is not a case "where the judgment of the state court rests on two grounds, one involving a federal question and the other not," *Lynch v. New York*, 293 U. S. 52, 55, *Utley v. St. Petersburg*, 292

U. S. 106, 112; or one in which there is a "non-federal ground" "independent of the federal ground and adequate to support it," *Fox Film Corp. v. Muller*, 296 U. S. 207, cf. *Swiss Oil Corp. v. Shanks*, 273 U. S. 407; or one in which there is a "non-federal ground" "so interwoven with the other as not to be an independent matter," *Fox Film Corp. v. Muller*, 296 U. S. 207, *Enterprise Irr. Dist. v. Farmers Mutual Canal Co.*, 243 U. S. 157; *Creswill v. Knights of Pythias*, 225 U. S. 246, infra p. 60, *Abie State Bank v. Bryan*, 282 U. S. 765; or, one in which it is necessary to consider whether a denial on non-federal grounds of claimed constitutional protection "rests upon a fair and substantial basis," *Lawrence v. State Tax Comm.*, 286 U. S., 276, 280-282; *Broad River Power Co. v. South Carolina*, 281 U. S. 537, 540; *Ward v. Love County*, 253 U. S. 17, *Klinger v. Missouri*, 80 U. S. 257; or is "so plainly unfounded that it may be regarded as essentially arbitrary or a mere device to prevent the review of a decision upon the federal question," *McCoy v. Shaw*, 277 U. S. 302; or one in which the constitutional issue was evaded, *Fox River Paper Co. v. Railroad Commission*, 274 U. S. 651; or one in which the federal ground might have been considered by the state court, but was not, *Grayson v. Harris* 267 U. S. 352; or one in which "the Federal right has been denied as the result of a finding of fact it is contended there was no evidence to support," *Creswill v. Knights of Pythias*, supra,—although any other view of the opinion of the court than the one we have, puts it in the class with those cases in which the federal question is so interwoven as not to be an independent matter; in which the decision does not rest upon a fair and substantial basis and is so illusory that it may

be regarded as essentially arbitrary or a device to prevent the review of a decision upon the federal question; in which the constitutional issue was evaded, and those in which the findings upon which the holding rests are contrary to the undisputed evidence and without any support in the record.

There is nothing in this case of an independent nature like the question of severability of the parts of a contract, *Fox Film Corp. v. Muller*, 296 U. S. 207, of waiver, *Eustis v. Bolles*, 150 U. S. 361, *Harding v. Illinois*, 196 U. S. 78, or whether the federal right was prematurely asserted, *Petrie v. Nampa & M. Irr. Dist.*, 248 U. S. 154, or the validity of a contract under state law, *Vandalia R. Co. v. Indiana*, 207 U. S. 359, or of the adequacy of a legal remedy, *McCoy v. Shaw*, 277 U. S. 302, or of the effect of a voluntary payment of taxes, *Gaar, Scott & Co. v. Shannon*, 223 U. S. 468.

On the contrary, this is a case in which appellants cannot be held liable for the tax, as an occupation tax, consistently with the Federal Constitution, on any ground, *Logan Bank v. Townsend*, 139 U. S. 67; it is one in which the judgment could not have been given without deciding the Constitutional questions presented, *Murray v. Charleston*, 96 U. S. 432, *Eustis v. Bolles*, 150 U. S. 361, *Meyer v. Richmond*, 172 U. S. 82, *Gaar Scott & Co. v. Shannon*, 223 U. S. 468, *Harding v. Illinois*, 196 U.S. 78. It is one in which the state court puts its decision denying the federal right claimed upon an erroneous view of the law, *Columbia R. G. & E. Co. v. South Carolina*, 261 U. S. 236, *Grayson v. Harris*, 267 U. S. 352, *Terre Haute & I. R. Co. v. Indiana*, 194 U. S. 579, cf. *Macallen v. Massachusetts*, 279

U. S. 620, *Dorchy v. Kansas*, 272 U. S. 306, and in which the decision of the state questions was preliminary and related to the Federal right only in the sense that it brought the case within the reach of the Federal law relied on, *Grayson v. Harris*, supra.

The jurisdiction does not rest upon surmise, *Lynch v. New York*, supra. The State court clearly held the law could not be sustained as a property tax under the State Constitution, thus leaving for determination the question of its constitutionality as an occupation tax under the identical due process and obligation of contract clauses of the State and Federal Constitution — of which the latter is supreme, *Swiss Oil Corp. v. Shanks*, 273 U. S. 407.

Appellants, not being engaged in the business or occupation of producing oil, and being royalty owners under leases requiring the lessee to pay the expenses of engaging in the business, challenged the law as violating the due process clause of the fourteenth amendment to, and the obligation of contract clause of the Federal Constitution. The Texas courts held the Legislature had power to declare them engaged in the business, *whether they were or not*, and that the fact the law compelled them to bear part of their lessee's expenses did not impair the obligation of the leases. Such holding directly disposes of the Constitutional attack.

The challenged legislation is novel. No similar legislation has ever been sustained by this court. The constitutional questions involved are substantial, *Fiske v. Kansas*, supra, *Sultan Ry. v. Department of Labor*, supra, *Sprout v. South Bend*, supra, *Salinger v. United States*, 272 U. S. 542, *Aetna Life Ins. Co.*

v. Dunken, 266 U. S. 389, and are not lacking in substance within the meaning of *Corrigan v. Buckley*, 271 U. S. 323, *Roberts v. Emmerson*, 271 U. S. 50, *Edward Hines Trustees v. United States*, 263 U. S. 143, and *Zucht v. King*, supra.

The judgment of the Court of Civil Appeals was entered November 13, 1935, (R. 37) motion for rehearing in that court was overruled December 18, 1935, (R. 40) petition for writ of error to the Supreme Court of Texas was denied, February 5, 1936, (R. 42) and motion for rehearing overruled February 26, 1936, (R. 44). Petition for appeal to this court (R. 57) was filed and allowed March 7, 1936, (R. 60) and the record filed in the Clerk's office here March 12, 1936. The petition for appeal was accompanied by the required assignment of errors (R. 58) and the jurisdictional statement (R. 60).

This court has jurisdiction of appeals from the highest court of a state in which a decision can be had, upholding a law where its validity under the Federal Constitution is drawn in question, 28 U. S. C. 344, 861, *Sultan Ry. v. Dept. of Labor*, 277 U. S. 135, *Sprout v. South Bend*, 277 U. S. 163, *Atlantic Coast Line v. Goldsboro*, 232 U. S. 548, *Zucht v. King*, supra, when applied for within three months, 28 U. S. C. 350.

When a Court of Civil Appeals of Texas affirms a judgment "the judgment * * * rendered * * * shall be final" and "the lower court from which the cause was removed need not make any further order or decree therein." *Vernon's Annotated Texas Statutes*, Art. 1857, 1858.

While the Supreme Court of Texas has jurisdiction to review cases from the Courts of Civil Appeals "involving the construction or the validity of statutes" and is required to refuse an application for writ of error "where the judgment of the Court of Civil Appeals is a correct one and where the principle of law declared in the opinion of the court is correctly determined," *Vernon's Annotated Texas Statutes*, Art. 1728, as amended, "the refusal or dismissal of an application" has "the effect of denying the admission of the cause into the Supreme Court" and such "refusal * * * shall not be regarded as a precedent or an authority," *Vernon's Annotated Texas Statutes*, Art. 1750.

It was necessary for appellants to invoke the jurisdiction of the Supreme Court of Texas in order to make it certain that the case could go no further, *Stratton v. Stratton*, 239 U. S. 55, but, when the Supreme Court declined to admit the case, the Court of Civil Appeals became the highest court of the state in which a decision could be had, *American Ry. Express Co. v. Levee*, 263 U. S. 19, *Matthews v. Huwe*, 269 U. S. 262, and in this situation this court has always considered the Texas Courts of Civil Appeals as the highest state court, *Sullivan v. Texas*, 207 U. S. 416, *Bacon v. Texas*, 163 U. S. 207, *St. Louis, S. F. & T. R. R. Co. v. Seale*, 229 U. S. 156, *Zucht v. King*, 260 U. S. 174. This is especially true where on the refusal to admit a case to the high state court the record is returned to the intermediate court (R. 60). *Hodges v. Snyder* 261 U. S. 600, *Rothschild v. Knight*, 184 U. S. 334, *McDonald v. Massachusetts*, 180 U. S. 311.

The appeal was allowed within three months of the entry of the order overruling appellants' motion for rehearing in the Court of Civil Appeals, *Morse v. United States*, 270 U. S. 151, *United States v. Ellicott*, 223 U. S. 524, *Kingman & Co. v. Western Mfg. Co.*, 170 U. S. 675, *Aspen Mining & Smelting Co. v. Billings*, 150 U. S. 31, but it would have been in time if it had been applied for within three months after the Supreme Court of Texas finally acted, *American Ry. Express Co. v. Levee*, supra.

The case is properly here for consideration of the validity of the law both in terms and as applied, *Fiske v. Kansas*, 274 U. S. 380, *Dahnke-Walker Co. v. Bondurant*, 257 U. S. 282.

STATEMENT OF THE CASE

This case involves the constitutionality, under the due process clause of the Fourteenth Amendment and the obligation of contract clause of Article 1, Section 10 of the Federal Constitution, of a law of Texas enacted in 1933, requiring the owners of royalty under oil leases to bear part of the occupation tax levied upon the privilege of engaging in the business of producing oil. The law is challenged as violating the foregoing provisions of the Constitution both in terms (R. 9) and as applied (R. 10).

From 1919 to 1933 "each person owning, controlling, managing, operating or leasing * * * any oil well, or any person who produces in any other manner any oil by taking it from the earth" was required to report the total production quarterly and pay an occupation tax of two per cent of the amount of oil pro-

duced.[1] This law was construed as levying the entire tax upon the lessee producer and none of it upon the royalty owner. (R. 3 and Agreed Facts (R. 31-35).

While this law was in force and on May 11, 1925, Mrs. M. M. Cook, lessor, gave oil leases on part of the Cook Ranch in Shackelford County, Texas, to Roeser & Pendleton, Inc., lessee, by which the lessee "acquired the right, exclusive of everyone, including the lessor, to go upon" and "produce and save oil and gas from said land." The leases provide, as lessor's royalty, for delivery "to the credit of lessor *free of cost*, in the pipe line to which it may connect its wells, the equal one-eighth part of all oil produced," (R. 2, 19-22).

After said leases had been in effect eight years, during all of which time lessee paid the entire 2% gross production tax required under the provisions of the above law, it was amended by H. B. 154, Acts 1933, 43rd Legs. p. 409, ch. 162, and again amended by Acts 1933, 43rd Legs. 1st C. S. p. 43, ch. 12, Vernon's Annotated Texas Statutes 1925, Supp. Art. 7075-A. The amended law in question now levies what is denominated "an occupation tax on oil produced within this State of two cents per barrel." It is provided that the tax "*shall be borne ratably by all interested parties, including royalty interests*" and producers and purchasers are required to withhold from any payments due interested parties, the proportionate tax due, report and pay same to appellee, the Comptroller, who delivers the remittances to the appellee State Treasurer for credit to the proper state fund.

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1. Vernon's Annotated Texas Statutes, Art. 7071, appendix B hereto.

Since this suit was filed, by amendment in 1935 the definition of "producer" was made to include "*any person owning any royalty* or other interest in any oil or its value *whether produced by him, or by some other person on his behalf, either by lease, contract or otherwise.*"[1]

The case was tried (R. 35) upon an agreed Statement of Facts (R. 15), which stipulates that neither Mrs. Cook nor the trustees of her estate

> "ever exercised or attempted to exercise, any degree of control over oil operations on said Cook Ranch; and at no time has either Mrs. Cook or the Trustees of her estate ever produced any oil from the Cook Ranch, or ever been in the occupation of producing oil from the Cook Ranch, but on the contrary Roeser & Pendleton, Inc., and its assigns, have been the sole and exclusive producers of oil and gas from said Cook Ranch, and no other person, save Roeser & Pendleton, Inc. and its assigns, has been engaged in such occupation named. In connection with the foregoing, and in using the phrase, 'Roeser & Pendleton, Inc., and its assigns,' it is meant to include in said term the assigns of Roeser & Pendleton, Inc., but neither Mrs. Cook nor the trustees of her estate, has been such assigns, but they have at all times been merely the owner of substantially one-half of the royalty oil produced from the Cook Ranch by Roeser & Pendleton, Inc., lessee and its assigns, (R. 27. To the same effect see allegations in plaintiffs' petition, R. 7.)
>
> "That neither Mrs. W. I. Cook, during her lifetime, nor the executors or trustees of her estate,

1. The challenged enactment and the amendments are set out in full in Appendix A hereto.

have ever been producers, managers or operators of the oil property upon the Cook Ranch, but at all times since the discovery well was brought in, in 1926, Roeser & Pendleton, Inc., the lessee, and its assigns, have been the exclusive producers, managers and operators of said property.

"That at all times since the discovery well was brought in in February, 1926, Roeser & Pendleton, Inc., lessees, and its assigns, have had the exclusive right to enter upon the Cook Ranch and explore, manage, develop and operate the same for oil and gas, and to produce and save oil therefrom, being accountable to Mrs. Cook and to the executors and trustees of her estate, for her and their part of the royalty oil and gas provided for in the leases hereinbefore mentioned.

"That at no time since the discovery well was brought in on the Cook Ranch in February, 1926, has either Mrs. Cook or her executors or Trustees ever been engaged in the occupation or business of producing oil from the Cook Ranch or elsewhere, but on the contrary, have merely received from the purchaser, the purchase price for their part of the royalty oil produced from said Cook Ranch by Roeser & Pendleton, Inc., lessee, and its assigns." (R. 31).

Appellants' lessee connected its wells to the pipe line of the Humble Oil & Refining Company and the oil was delivered to it on division orders effective in 1932, providing for payment of the regular posted price for the oil, (R. 27-28). The purchaser of the oil was notified by the Comptroller to comply with the law (R. 7) and it in turn advised appellants that, pursuant to the challenged enactment it would deduct from appellants' remittances and pay the State officials the proportionate part of the tax (R. 29-30).

Appellants requested the purchaser to withhold payment of the tax (R. 32-33) and were advised that unless it was permitted to make the payment, arrangements would have to be made to segregate and deliver to appellants their part of the oil (R. 32-34). The Humble Company continued making payments of the tax under protest and the refund sued for herein has since been held in suspense, (R. 18-19).

A former suit to enjoin the enforcement of the taxing act was dismissed by the Federal Court because the requisite jurisdictional amount was not involved, 8 *Fed. Supp.* 21, Id. 293 U. S. 527. This suit in the State Court followed.

In their petition appellants, after pleading the facts, substantially as stated, allege that said law violates the due process clause of the Fourteenth Amendment and the obligation of contract clause of the Federal Constitution because: (a) While appellants are not engaged in the business or occupation of producing oil they are arbitrarily defined to be so engaged and are taxed accordingly, and (b) part of the royalty payable to them under their leases is appropriated for the benefit of their lessee, in violation of the lease contract (R. 1-10). While not involved in this appeal they also alleged the tax is in reality a property tax and as such is violative of provisions of the Texas Constitution[1] requiring that property taxes be equal and uniform, limit them in amount to thirty-five cents on the One Hundred Dollar valuation, require rendition, assessment and payment of such taxes in the

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1. The Constitutional provisions are Appendix C pp. 53-54.

county where the property is situated and the equalization of values for tax purposes by the several County Commissioners' courts;[1] alleging in that connection that these ad valorem taxes on their royalty interest had been assessed and paid in Shackleford County, (R. 11). They prayed for an accounting and refund of the amount held in suspense,[2] and an injunction against the enforcement of the law, (R. 13-14).

Appellees' answer was a general demurrer and general denial, (R. 15) the cause was heard upon the pleadings and the agreed statement of facts (R. 15-35). The trial court held the law constitutional, sustained the general demurrer to appellants' petition and dismissed the suit (R. 35).

Appellants appealed to the Court of Civil Appeals, where they assigned as error the holding of the trial court that said gross production tax law did not violate the mentioned provisions of the Federal Constitution, (R. 36-37). The Court of Civil Appeals affirmed the judgment of the trial court. At the same time it decided another case involving similar questions, and the two opinions, (R. 45-57) 89 S. W. (2) 1021-1037 may be summarized as follows:

> "We construe the act to levy this tax against the various interest holders in the oil produced, including the producer and royalty owners * * * in proportion to their respective interests" and that as thus construed the act is valid and constitutional. "We also hold that for the purpose

1. See Sheffield v. Hogg, infra p. 54.

2. The law authorizing suit for the refund is Appendix D hereto, p. 55.

of levying a gross production or occupation tax on oil, *the Legislature may validly declare the owners of royalty interests in the oil produced to be engaged in the occupation or business of producing oil.*"

The tax is "levied ratably or in proportion to the interest each party has in the oil produced." The law "does not mean that the tax is levied only against the producer." The law does "not levy the tax against the purchaser. He is merely made the agent of the State to collect from the producer or other interest holders the total amount of the tax due; and he is authorized to charge their respective accounts with the proportionate tax due." "Whatever the character of the lease * * * there is always reserved a royalty interest * * * and manifestly this is the 'royalty interest' within the contemplation of the taxing act in suit, and against the owner of which the tax was levied."

"The tax is not dependent upon the character of title under which the producer produces the oil. Nor is the tax levied on the oil in place. *The tax is levied on the business or occupation of producing the oil.*" The act provides that the "royalty interest would be taxed against the owner or holder of the royalty interest."

"We are also clear in the view that for the purpose of levying the gross production tax on the occupation or business of producing oil, *the Legislature may validly declare the owners of royalty or other interests in the oil produced to be engaged in the occupation or business of producing oil.* The ordinary form of oil lease has a dual character or purpose: (1) The conveyance of an estate in the land for development purposes; and (2) the future development and operation of the lease for oil in accordance with the terms, ex-

press and implied, of the contract for the mutual benefit of the parties, their respective benefit being measured by the extent of their interests in the oil produced, or its value. The law is settled that the primary objective or purpose of the oil lease is the production of oil for the mutual profit of the parties. The consideration moving to the lessor is an interest in the oil or its value in money. Thus he has a direct interest in the success of the business. As the holder of the royalty interest the lessor or royalty owner is not only entitled to share in the gross production of the oil, but may under the terms of the lease, expressed or implied, require proper, prudent, and diligent management and development of the business, and has reserved and is entitled to both legal and equitable remedies necessary to enforce the obligations of the lease, and under some circumstances may forfeit the lease for non-development.

"The tax of two cents per barrel on oil produced is a gross production or gross receipts tax, the amount of the tax being measured by the gross activity of the business, *and is under the authorities an occupation tax.* Since the taxing act in suit contempated a tax on gross production of oil, the amount of the levy being measured or determined by the gross receipts of the oil or business, we conclude that the Legislature may reasonably impose the tax burden on those entitled to share in the gross receipts or profits of the oil enterprise, particularly so since under the lease contracts royalty owners may enforce its express and implied covenants, looking to the proper and diligent development and management of the business, to the end that their share in the receipts will increase and produce a greater royalty interest in the business."

"Appellants contend that the taxing act in suit

is violative of the obligation of contract clauses of both the State and Federal Constitutions. This taxing act does not change in any manner the lease contracts between the parties. *The tax is not against the oil royalty. It is levied as a gross production tax on the business or occupation of producing oil.* The tax belongs to the State, and the mere fact that the producer is primarily liable for the payment of the tax, or the fact that the purchaser is required to collect the tax for the State at its source or origin, does not give them any interest in the tax against the royalty interests. They may have benefited by the change of legislative policy of imposing the tax ratably against the respective interest holders in the oil produced; but such legislative tax policy did not impair any obligation of the lease contracts.

"In this connection appellants cite several cases in support of the contention that royalty owners under the ordinary form of oil and gas leases are not engaged in the business of producing oil. * * * *The Legislature may validly declare the owners of royalty interests in the oil produced to be engaged in the business or occupation of producing oil for the purpose of levying the occupation tax against them.*"

The assigned errors (R. 58-59) are as follows:

1. The Court of Civil Appeals erred in holding the Legislature and appellees could, consistently with the due process clause of the Federal Constitution, arbitrarily provide and say in and under the law in question that appellants are engaged in the business of producing oil, when they are not in fact so engaged, in order to lay upon them a tax for which they could not be held liable, unless they were so engaged.

2. Appellants antecedent leases having obligated the lessee to deliver appellants' royalty oil to their credit in the pipe line free of cost, the Court of Civil Appeals erred in holding that the obligation of said leases was not impaired in violation of the obligation of contract and due process clauses of the Federal Constitution, by the tax law in question, which authorizes and requires the deduction of two per cent of the proceeds of lessor's oil, which relieves the lessee of a part of the cost of producing the oil, makes the appellants' royalty interest less valuable, and the method of enforcing the lease entirely different than when it was made.

3. The Court of Civil Appeals erred in holding the law in question does not contravene the provisions of the Federal Constitution mentioned in plaintiffs' petition.

4. The Court of Civil Appeals erred in holding appellants were not entitled to recover the taxes exacted, and to enjoin the future taxes assessed under the laws in question.

We submit the following (R. 61):

POINTS

I

It being an admitted fact that appellants are not engaged in the business of producing oil, the Texas Gross Production Tax law of 1933, as amended, which arbitrarily provides that they are engaged in such business, to lay an otherwise prohibited tax upon them, contravenes the due process clause of the Fourteenth Amendment to the Federal Constitution.

II

Appellants antecedent leases having obligated the lessee to deliver appellants' royalty oil to their credit in the pipe line free of cost, the tax law in question which authorizes and requires the deduction of two per cent of the proceeds of appellants' oil and the addition of a like amount to the proceeds of their lessees' oil, which relieves the lessee of a part of the cost of producing the oil, makes the appellants' royalty interest less valuable, and the method of enforcing the lease entirely different than when it was made, violates the due process clause of the Fourteenth Amendment to, and the obligation of contract clause of the Federal Constitution.

ARGUMENT[1]

The State Court, basing its holding on rules which could apply only if the law levied a property tax, held the law levied the tax upon the occupation or business of producing oil. It treated the tax as if it were levied on the active engaging in the business or occupation of producing oil, and said it was properly made payable by those owning the oil, in proportion to their respective interests therein, irrespective of their activity in the business or occupation. It did not find that appellants, who are royalty owners and admittedly are not engaged in the business or occupation of producing oil, were in fact engaged therein, but undertook to justify their treatment as producers, by saying their right to receive royalty, to enforce the express and implied covenants of the lease, and the

1. Most of the authorities cited in this argument are alphabetically arranged, analyzed and quoted from in Appendix E hereto.

mutual benefit which results to all parties from fulfillment of the lease contract, gave them a "direct interest in the success of the business."

Its holding means that while the tax is an occupation tax on the business of producing oil, it loses none of its characteristics when it is spread on all who have an interest in the oil, solely because of such interest therein and irrespective of their lack of activity in the business. If one of the parties interested in the oil has to pay a tax for producing it, everyone else interested in it has to pay a part of the tax, regardless of whether or not he engages in the business taxed.

While the construction of state statutes and constitutions, and the rights of parties under contracts, are questions of local law on which the decision of the state court is ordinarily final, *Fox River Paper Co. v. Railroad Commission*, 274 U. S. 651, *Swiss Oil Corporation v. Shanks*, 273 U. S. 407, *Sauer v. New York*, 206 U. S. 536, *Vandalia R. Co. v. Indiana*, 207 U. S. 359, cf. *Dorchy v. Kansas*, 272 U. S. 306, the effect of a law on rights secured by the Federal Constitution cannot be foreclosed by a decision of the state courts, *Educational Film Corporation v. Ward*, 282 U. S. 379. This Court determines for itself the nature and effect of a tax, regardless of the definition of it by the state court, *Lawrence v. State Tax Commission*, 286 U. S. 276, 282, *Educational Film Corporation v. Ward*, supra, *Macallen v. Massachusetts*, 279 U. S. 620, 625, *G. H. & S. A. Ry. Co. v. Texas*, 210 U. S. 217, *Murray v. Charleston*, 96 U. S. 432. *Appleby v. New York*, 271 U. S. 364, especially where the State court, clearly relying on the uncon-

stitutional legislation, bases its decision on an untenable view of the rights and situation of the parties, *Columbia R. G. & E. Co. v. South Carolina*, 261 U. S. 236, *Terre Haute & I. R. Co. v. Indiana*, 194 U. S. 579, which is entirely without support in the evidence, cf. *Creswill v. Knights of Pythias*, 225 U. S. 246, *B. & W. Taxi Co. v. B. & Y. Taxi Co.*, 276 U. S. 529-30.

FIRST: Appellants' petition alleges they are not engaged in the business or occupation of producing oil. Appellees' demurrer, which was sustained to the petition, admits these allegations to be true. The portions of the agreed statement of facts which we have copied in the statement of the case (supra pp. 11-12). show that appellants have no part in the business or occupation of producing oil from the leased premises.

Under the leases they have no right to participate or engage in the business of producing oil on the leased premises. "By the agreement (the leases) the exclusive right to take and appropriate all the minerals is conveyed and during the term of the lease the lessor has no right to enter and operate for oil," *Barnsdall v. Bradford Gas Company*, 225 Pa. 343, 74 A 207, 26 L. R. A. (N. S.) 614. "The *lessee* had the right to take *full* charge of the land so far as necessary to get the oil from under it." *Japhet v. McRae*, (Com. Apps. Tex.) 276 S. W. 669, 671. An oil lease confers "on the lessee the essentials of ownership: possession with unrestricted power of appropriation * * * of the oil," *Waggoner Estate v. Wichita County*, 273 U. S. 113, which follows *Japhet v. McRae*, supra, and *Barnsdall v. Bradford Gas Co.*, supra. These cases are discussed and followed in *Sheffield v. Hogg* (Tex. Sup.) 77 S. W. (2) 1021, 1026-

1027. cf. *Sauder v. Mid-Continent Petroleum Corpn.*, 292 U. S. 272.

These cases make it plain that a Texas oil and gas lease, first, reserves to the lessor an estate in the land to the extent of the royalty reserved and divests out of lessor all right to engage in the business of producing oil on the premises during the life of the lease; and, second, it vests in the lessee title to all the oil in place, except the reserved royalty, and vests in the lessee the exclusive right to go upon the premises and there engage in the business of producing oil. As shortly stated by the same court from which this appeal was taken, in *Shell Pet. Corp. v. State*, 86 S. W. (2) 245, 249, where an oil lease has been executed the lessor "has parted with every title and interest in land except that of a royalty holder of minerals under a mineral lease which accords to the lessee the full right of development and consequently of possession," and "the interest reserved is" not sufficient to support an action in trespass to try title, in which under the Texas law, plaintiff must show he was in possession or entitled to possession, *Vernon's Annotated Texas Statutes*, Art. 7365, *State v. Dayton Lumber Co.*, 106 Tex. 41, 155 S. W. 1178.

Nevertheless, appellees, purporting to act under the challenged law, have declared appellants are engaged in the business or occupation of producing oil, in order to collect this so-called occupation tax from them, notwithstanding they are not engaged in such business or occupation, in fact, and have no legal right to engage therein, under the leases.

While the Court of Civil Appeals says the tax on appellants is an occupation tax, levied on the business

or occupation of producing oil, it points to no *activity in relation to the business of producing oil*, which a lessor can engage in. Indeed, there is none. It says, however, that appellants own the royalty and have contractual rights under the lease, which justify calling lessors producers. This is where it errs, for these rights are the rights of an *owner*, not evidence that one is engaged actively in business.

The *right* of the lessor *to have the royalty paid*, and *his right to enforce* the express and implied *covenants* of the lease, *are incidents of ownership*. A tax upon them would be a tax upon property. "To levy a tax by reason of ownership is to tax the property * * * it cannot be made an occupation or excise tax by calling it so." *Dawson v. Kentucky Distilleries, etc., Co.*, 255 U. S. 288. "A tax upon property holders in respect of their estate, whether real or personal, or of income yielded by such estate, and the payment of which cannot be avoided, are direct taxes." "It has always been considered that a tax upon real estate eo nomine, *or upon its owners in respect thereof is a direct tax.*" "We are unable to conclude that the enforced subtraction from the yield of all the owner's real or personal property * * * is so different from a tax upon the property itself, that it is not a direct but an indirect tax," *Pollock v. Farmers Loan & Trust Co.*, 157 U. S. 429, Id. 158 U. S. 601.

On the other hand "the requirement to pay" a privilege tax "*involves the exercise of privileges* and the element of absolute and unavoidable demand is lacking." *Flint v. Stone Tracy Co.*, 220 U. S. 107. "The distinction lies between the attempt to tax the property as such, and to measure a legitimate tax upon

the privileges enjoyed in the use of such property." *Western Union Tel. Co. v. Kansas*, 216 U. S. 1. "The difference * * * is not merely nominal but rests upon substantial differences between the ownership of property and the *active doing of business in a certain way.*" *Flint v. Stone Tracy Co.*, supra.

Zonne v. Minneapolis Syndicate, 220 U. S. 187, *McCoach v. Minehill S. & H. Co.*, 228 U. S. 295, *United States v. Emery Bird, Thayer R. Co.*, 237 U. S. 28, all hold that corporations not engaged in business, *but merely receiving rents from their property*, are not liable to pay the excise tax on corporations "engaged in business."

To lay a tax upon the lessor because of the legal and equitable rights and remedies which he has for the enforcement of the express or implied obligations of an oil lease is, under the rule of the cases cited, to tax the property itself. This is the thing the Court of Civil Appeals says cannot constitutionally be, and was not done, but the holding involves a *contradiction*. The ordinary incident of an occupation tax, is the actual doing of business of the kind taxed. This the court ignores, and, in the same breath it says the tax is an occupation tax, it turns to the principles of property taxation and says the tax is justified because of nothing more than the property rights of the lessor under the lease.

> "The words of the act and the opinion of the state court as to the nature of the tax are to be given consideration and weight; but they are not conclusive. As it many times has been decided, neither state courts nor legislatures, by giving the tax a particular name, or by using some form of words, can take away our duty to consider its

nature and effect. Choctaw, O. & G. R. Co. v. Harrison, 235 U. S. 292, Galveston, H. & S. A. R. Co. v. Texas, 210 U. S. 217. And this court must determine for itself by independent inquiry whether the tax here is what, in form and by the decision of the state court, it is declared to be, namely, an excise tax on the privilege of doing business, or, under the guise of that designation, is in substance and reality a tax on the income derived from tax exempt securities. If, by varying the form,—that is, to say, if, by using one name for a tax instead of another, or imposing a tax in terms upon one subject when another is in reality aimed at, the substance and effect of the imposition may be changed, constitutional limitations upon powers of taxation would come to naught." *Macallen v. Massachusetts*, 279 U. S. 620.

The ruling in the cited case is applicable. Here the State, because of constitutional limitations, *Sheffield v. Hogg*, 77 S. W. (2) 1021, infra p. 54, cf. *Swiss Oil Corporation v. Shanks*, 273 U. S. 407, is denied the right to levy the tax directly, as a tax on the royalty interest. This much the state courts concede. However the courts join the legislature and appellees in declaring that "*for the purpose of levying a gross production or occupation tax on oil, the legislature may validly declare the owners of royalty interests in the oil produced to be engaged in the occupation or business of producing oil.*" This declaration is made, we repeat, in face of the agreed and admitted fact that the appellants are not so engaged, and under the terms of their leases, as construed by the Texas courts, they have no right to engage therein, or to have possession of the property for such purpose, during the term of the lease. The evasion in this is

apparent, but it is the evasion which brings the law and decision into constitutional difficulty.

The requirement to pay an occupation tax can be predicated only upon the exercise of the privilege taxed. Lessors not enjoying or exercising that privilege cannot, consistently with due process, be compelled to pay it, by a mere definition. "While the lawmaker is entirely free to ignore the ordinary meaning of words and make definitions of his own * * * that device may not be employed so as to change the nature of the acts or things to which the words are applied," *Carter v. Carter Coal Co.*, 297 U. S. ..... Occupation taxes or excises may be levied upon proper subjects, but the legislative power cannot, consistently with due process, be employed to arbitrarily create the conditions under which liability shall exist, irrespective of the truth. To define as producers people who are not producers, in order to levy a producer's privilege tax upon them is the grossest sort of confiscation. "Mere legislative fiat may not take the place of facts in the determination of issues involving life, liberty or property." *Manley v. Georgia*, 279 U. S. 1, cf. *Dawson v. Kentucky Distilleries*, supra.

The Legislature cannot for the same reasons ignore substantial facts and say all carriers for hire are common carriers, *Smith v. Cahoon*, 283 U. S. 553; *Frost v. R. R. Comm. of Cal.*, 271 U. S. 583; *Mich. Comm. v. Duke*, 266 U. S. 570; *Washington v. Kuykendall*, 275 U. S. 207, cf. *Stephenson v. Binford*, 287 U. S. 251, or by legislative fiat create a conclusive presumption, *Schlesinger v. Wis.*, 270 U. S. 230, or by the same means convert a private business into a public utility, *Producers Trans. Co. v. R. R. Comm.*, 251 U. S. 228, 230, as the ice business, *New State Ice Co. v. Leib-*

mann, 285 U. S. 262; or declare business affected with a public interest, *Tyson & Bro. v. Banton*, 273 U. S. 418. See also *Eisner v. Macomber*, 252 U. S. 189, where Congress was held to be without power to say that stock dividends were income, when they are not such in fact. So in *Weaver v. Palmer Bros.*, 270 U. S. 402, it was held a law prohibiting the use of shoddy in the manufacture of bedding was unconstitutional as applied, when it was shown shoddy was not dangerous to health when sterilized, notwithstanding the Legislature's declaration to the contrary. And, in *Carter v. Carter Coal Co.*, supra, a penalty was held to be such regardless of the fact Congress called it a tax and a congressional declaration that the Guffey Coal Act regulated interstate commerce was set aside when it appeared such was not its substantial effect.

These illustrations bring to mind a statement once made by Daniel Webster:

> "I have only to remark that neither a preamble, nor any other declaration of a legislative body, can create a fact or alter a fact. I remember to have heard Chief Justice Marshall ask counsel who was insisting upon the authority of an act of legislation if he thought an act of legislation could create or destroy a fact, or change the truth of history. Would it alter the fact, said he, if a legislature should solemnly enact, that Mr. Hume never wrote the history of England? A legislature may alter the law but no power can reverse a fact." Vol. 2, Webster's Works (1851) page 334.

SECOND: The law violates the obligation of contract clause. Of course, if the question were simply one of taxing property or privileges appellants owned

and enjoyed, they could not escape the taxing power, *Lake Superior Consolidated Mines v. Lord*, 271 U. S. 577, 581. Such is not the case.

Appellants conveyed to their lessee the exclusive right to engage in the business of producing oil on the leased land. The lessee agreed to bear the cost of enjoying that privilege. For eight years the lessee paid the gross production tax on all oil produced. Then the Legislature amended the law, and in the face of our contract, says lessor must now bear a part of the same occupation tax. It ignores the fact the lessee voluntarily assumed and for years bore this burden, under the terms of the lease and could not require appellants to bear part of it.

The obvious purpose of the challenged law is to so spread the tax on the exclusive privilege enjoyed by the lessee, of engaging in the business of producing oil under the leases, or that lessees' tax burden will be lightened in the proportion that the lessee owns less than one hundred per cent of the oil, at lessor's expense.

Under the law an amount equal to 1/8th of 2% is inevitably added to the lessee's income under the lease. This identical sum is taken from the income the lessor is entitled to under the terms of the lease. The lessee now delivers the royalty oil to the pipe line, charged with a part of the tax on its privilege of engaging in the business of producing oil, not "free of cost" as the lease stipulates.

Aside from the fact that this is taking one man's property and giving it to another, both the taking and giving are directly in the teeth of a written obli-

gation, voluntarily assumed by the one thus benefitted. The lease obligates the lessee to pay the tax on the exclusive privilege enjoyed by him of engaging in the business or occupation of producing oil on the leased premises. This is the obligation the State has no right to impair; it is the obligation impaired by the law in question.

> "A change of the expressed stipulations of a contract, or a relief of a debtor from strict and literal compliance with its requirements, can no more be effected by an exertion of the taxing power than it can be by the exertion of any other power of a State Legislature. The constitutional provision against impairing contract obligations is a limitation upon the taxing power, as well as upon all legislation, whatever form it may assume. Indeed, attempted state taxation is the mode most frequently adopted to affect contracts contrary to the constitutional inhibition. It most frequently calls for the exercise of our supervisory power."

> "The State may undoubtedly tax" a creditor "if its promise be left unchanged. A tax thus laid impairs no obligation assumed. It leaves the contract untouched. But until payment of the debt or interest has been made, as stipulated, we think no act of State sovereignty can work an exoneration from what has been promised to the creditor, namely: payment to him, without a violation of the Constitution." *Murray v. Charleston*, 96 U. S. 432.

Even if the law did no more than prescribe a *method* of spreading the tax, and left the lessor the right to collect the deducted amounts from the lessee—a speculation we cannot indulge—it would be bad for:

"The obligation of a contract depends upon its terms and the means which the law in existence at the time affords for its enforcement. A law which alters the terms of a contract by imposing new conditions, or dispensing with those expressed, is a law which impairs its obligation, for as stated on another occasion, such a law relieves the parties from the moral duty of performing the original stipulations of the contract, and it prevents their legal enforcement." *Cleveland P. & A. R. R. Co. v. Pennsylvania*, 15 Wall, 82 U. S. 300.

Cases recently decided, *Home Building & Loan Association v. Blaisdell*, 290 U. S. 298, *Langever v. Miller*, 76 S. W. (2) 1025, 96 A. L. R. 836, make it entirely plain that the obligation of the contract is violated, if its value is in anywise lessened or if the manner of enforcing it is materially changed, or if new burdens are added, or rights released, or lessened, or if remedies are made more onerous.

"There is no more important provision in the Federal Constitution than the one which prohibits states from passing laws impairing the obligation of contracts, and it is one of the highest duties of this court to take care the prohibition shall neither be evaded nor frittered away. Complete effect must be given to it in all its spirit. The inviolability of contracts, and the duty of performing them, as made, are foundations of all well ordered society and to prevent the removal or disturbance of these foundations was one of the great objects for which the Constitution was framed." *Murray v. Charleston*, supra.

CONCLUSION

We do not believe the Legislature had authority, consistently with due process, to ignore substantial facts and *"declare the owners of royalty interests in the oil produced to be engaged in the business or occupation of producing oil for the purpose of levying the occupation tax against them"* which, under the lease and law prior to its amendment was payable by the lessee. What the Court said in *Washington v. Kuykendall*, 275 U. S. 207, regarding a legislative declaration is apt: "They are common carriers, not because of legislative fiat, but by reason of the character of business they carry on. * * * A common carrier is such by virtue of his occupation, not by virtue of the responsibilities under which he rests." To which we add, he is such by virtue of his occupation and not by virtue of his property rights.

The Legislature did not intend by the amended law to increase or decrease the amount of the State's revenue, but clearly intended to relieve lessees of part of the burden they voluntarily assumed in making their leases, and put that burden on lessors, and to that extent deprive lessors of their revenue and rights under leases. The Constitution was designed to protect contracts from such impairment.

We respectfully submit the judgment of the Court of Civil Appeals should be reversed.

WILLIAM R. WATKINS,
Attorney for Appellants.

APPENDIX A

THE DANIEL PRODUCTION AND OCCUPATION TAX LAW

(Approved May 22, 1933)

H. B. No. 154

Be it enacted by the Legislature of the State of Texas:

SECTION 1.[1] (1) For the purpose of this Act "producer" shall mean any person or persons, corporation, partnership, individual, trustee, receiver, trust estate or administrator owning, controlling, managing, or leasing any oil well, or any person who produces in any manner any oil by taking it from the earth or waters in this State.

(2) "Purchaser" shall mean any individual, person, or persons, partnership, corporation, refinery, pipe line, or agent purchasing crude oil for any purpose or use within this State.

(3) "Carrier" shall mean the operator or owner of any means of transporting oil or any instrumentality that may now be used or come into use.

(4) "Oil" as used herein shall mean petroleum oil, mineral oil, or other oil taken from the earth.

(5) "Reports" shall mean any reports required to be furnished in this Act or that may be required by the Comptroller in the administration of this Act.

(6) "Person" shall mean and include any person, firm, concern, receiver, trustee, executor, administrator, agent, institution, association, partnership, company, corporation, and persons acting under declarations of trust as well as the trustees acting under such declarations of trust.

(7) "Production" or "total oil produced" shall mean the total gross amount of oil produced including all royalty or other interest; that is, the amount for the purpose of the tax imposed by this article shall be measured or determined by tank tables compiled to show one hundred per cent (100%) of the full capacity of tanks without deductions for base sedi-

1. Amended, infra p. 42.

ment, overage, losses in handling, or for any other purpose; or if amount of oil produced has been measured or determined by tank tables compiled to show less than one hundred per cent (100%) of the full capacity of tanks, then such amount shall be raised to a basis of one hundred per cent (100%) for the purpose of the tax imposed by this article.

(8) "Comptroller" shall mean Comptroller of Public Accounts of the State of Texas.

(9) "Commission" as used in this Act shall mean the Railroad Commission of Texas.

SEC. 2.[1] (1) There is hereby levied an *occupation tax* on oil produced within the State of two (2) cents per barrel of forty-two (42) standard gallons. Said tax shall be computed upon the total barrels of oil produced or salvaged from the earth or waters of this State without any deductions, and shall be based upon tank tables showing one hundred per cent (100%) of production and exact measurements of contents. Provided, however, that the occupation tax herein levied on oil shall be two per cent (2%) of the market value of said oil whenever the market value thereof is in excess of one dollar ($1) per barrel of forty-two (42) standard gallons. The market value of oil, as that term is herein used, shall be the actual value thereof, plus any bonus or premium, or other thing of value paid therefor or which such oil does or will reasonably bring, if produced in accordance with the laws, rules, and regulations of the State of Texas. (Italics ours).

(2) The tax hereby levied shall be a liability of the producer of oil and it shall be the duty of such producer to keep accurate records of all oil produced, making monthly reports under oath as hereinafter provided.

(3) The purchaser of oil shall pay the tax on all oil purchased and deduct tax so paid from payment due producer or other interest holder, making such payments so deducted to the Comptroller of Public Accounts by legal tender or cashier's check payable to the State Treasury.

Provided, that if oil produced is not sold during the month in which produced, then said producer shall pay the tax at the same rate and in the manner as if said oil were sold.

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1. Amended, infra p. 38.

(4) The tax herein levied shall be paid monthly on the 15th day of each month on all oil produced during the month next preceding by the purchaser or the producer, as the case may be, but in no event, shall a producer be relieved of responsibility for the tax until same shall have been paid; and provided, in event the amount of the tax herein levied shall be withheld by a purchaser from payments due a producer and said purchaser fails to make payment of the tax to the State as provided herein, the producer may bring legal action against such purchaser to recover the amount of tax so withheld, together with penalties and interest which may have accrued by failure to make payments and shall be entitled to reasonable attorney fees and court costs incurred by such legal action.

(5) Provided that unless such payment of tax on all oil produced during any month or fractional part thereof shall be made on or before the 15th of the month immediately following, such payment shall become delinquent and a penalty of 10 per cent (10%) of the amount of the tax shall be added; such tax and penalty shall bear interest at the rate of six per cent (6%) per annum from date due until date paid.

(6) The tax herein levied shall be borne ratably by all interested parties, including royalty interests; and producers and/or purchasers of oil are hereby authorized and required to withhold from any payments due interested parties, the proportionate tax due.

(7) The taxes herein provided for, when paid, shall be, and hereby are, allocated as follows, to-wit:

One-half of said tax when and as received by the Comptroller shall be paid to the State Treasurer of Texas and be placed to the credit of the Public School Fund, and one-half of such taxes when and as received by the Comptroller shall be paid to the State Treasurer to be placed to the credit of the General Fund of the State.

SEC. 3.[1] (1) Producers and/or purchasers of oil shall keep in Texas a complete record of all oil produced and a record of all oil sold; reports shall be filed with the Comptroller monthly by producers and purchasers, not later than the 15th of each

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1. Amended, infra pp. 40, 45.

calendar month, showing the amount of oil produced and the amount of oil sold during the month preceding, upon forms furnished by the Comptroller.

(2) All railroads, barges, trucks or pipe lines, carrying or transporting oil for hire, for themselves or their owners, shall keep in Texas a complete and accurate record of all oil so handled by months, showing date received, number of barrels, of whom received, point of delivery, to whom delivered and manner of transportation, and such records shall be open to the inspection of the duly authorized agents of the Comptroller or the Attorney General at all times, and, if requested by the Comptroller, shall furnish information and reports of movements as often as required by the Comptroller.

SEC. 4. Purchasers buying oil from properties in litigation or in receivership, bankruptcy, or any other legal proceedings, or covered by assignments, are required to deduct the amount of the taxes levied by this Act, before payment is made to the producers, trustees, assignees or to any person who claims ownership of said funds, or before the proceeds of said purchase of oil is impounded or escrowed by said purchaser pending such litigation or tenure of assignments, and shall remit said tax deducted in the same manner as if said oil had been purchased from any other source, and providing that said purchaser shall not be liable to any claimant of said funds on account of payment of said tax.

SEC. 5.[1] (1) Monthly reports by producers shall be filed with the Comptroller upon such forms as may be designated by that official, showing the total number of barrels of oil produced monthly, per well per calendar day, the name of the county from which produced, the name of the lease from which produced, the disposition made of such oil; if sold, the name and correct address of the purchaser, and if not sold, the location of storage, if owned by such operator, or if stored with a pipe line or a refinery, the correct name and address of such pipe line or refinery. All reports so made shall be duly sworn to by the producer or his authorized agent. The monthly report herein mentioned shall not be made on a per well per day

1. Amended, infra pp. 40, 48.

basis on wells producing an average of less than forty (40) barrels per day.

(2) Purchasers of oil shall accompany the remittance for taxes deducted from settlements as provided herein, with a statement or report in a form to be prescribed by the Comptroller, showing complete information requested in such form, including name and address of producer from whom oil was purchased; name of the county from which such oil was produced; name of the lease and the total number of barrels purchased.

SEC. 6.[1] For the occupation tax, penalties and interest herein provided for, the State shall have a prior and preferred lien on any leasehold interest, ownership of the oil rights, or interest, including oil produced and oil runs owned by the person owing any tax herein, and in addition thereto such lien shall include equipment, tools, tanks, and all other implements used on said lease from which oil is produced.

SEC. 7. It shall be the duty of the Attorney General to bring legal action for the collection of delinquent taxes herein levied, and a suit instituted shall attach to oil in storage, in transit, or being produced by such operator, and venue for such suits herein provided shall be in the district court of Travis County, Texas.

SEC. 8.[2] Whoever, as producer, purchaser, or carrier, or whoever, as the agent, employe, or representative of a producer, purchaser, or c rier, fails or refuses to comply with the provisions of this Act to keep records herein required to be kept, or whoever wilfully makes erroneous reports, as herein required to be made, or refuses to submit to examination of records by any authorized representative of the Comptroller or Attorney General, shall be guilty of a misdemeanor, and shall be punished by a fine of not less than twenty-five dollars ($25), nor more than five thousand dollars ($5,000), or confined in the county jail for not less than one (1) month nor more than six (6) months, or by both such fine and imprisonment.

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1. Amended, infra, p. 48.
2. Amended, infra p. 49.

SEC. 9.[1] It shall be the duty of the Comptroller to promulgate rules and regulations governing the detail administration of the terms and requirements of this Act not specifically mentioned herein; to employ auditors or tax supervisors for the purpose of verifying reports and investigating the affairs of producers and/or purchasers to determine whether the tax is being properly reported and paid; to provide necessary office help and equipment for the proper execution of the provisions of this Act, and for the purpose of defraying the necessary expense of said administration including salaries of supervisors, auditors, office help, filing equipment, typewriters and supplies, printing of forms, publication of regulations, postage, telephone and telegraph, travleing expenses of employees and traveling expenses of witnesses not otherwise paid, the amount of such expenses to be deducted from the gross amount collected monthly.

SEC. 9-a. Each and every person appointed by the commission and holding the certificate of the commission authorizing such appointee to inspect oil wells, oil leases, pipe lines, railroad cars, or tanks shall have the right of free access to such leases, premises, wells, pipe lines, railroad cars, or tanks, and to motor truck tanks, at any and all times for the purpose of inspection with respect to the production and transportation of oil. Any person or owner producing oil in this State who shall by objection, interference, or otherwise prevent any such person so appointed by the commission from the free right of access to any leases or premises or wells where oil is produced, or who shall in any manner interfere with such representative's examination of any such leases, premises, or wells to ascertain the quantity and time of production of oil, shall be guilty of a misdemeanor, and upon conviction thereof shall be subject to a fine of not exceeding five hundred dollars ($500) or by imprisonment in the county jail not exceeding six (6) months or by both such fine and imprisonment.

SEC. 9-b. It shall be unlawful for any person owning, leasing, operating, or controlling any oil property within the State of Texas to permit the oil or gas so produced to pass beyond the possession or control of such person into the possession or control of any other person without first accurately

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1. Amended, infra pp. 41, 49.

measuring the amount of such oil or such gas, and making and preserving an accurate record thereof. It shall also be unlawful for any person to use any method or device to evade such accurate measurement. Upon conviction for a wilful violation of any provision hereof, such person shall be deemed guilty of a felony and, upon such conviction, shall be punished by confinement in the State penitentiary for a term of not less than two (2) nor more than four (4) years.

Approved May 22, 1933.
Effective 90 days after adjournment.

(NOTE: H. B. No. 154 passed the House by a vote of 93 yeas, 26 nays; passed the Senate by a vote of 26 yeas, 2 nays. In approving this and H. B. No. 844 the Governor suggested appropriate legislation be enacted to harmonize the two laws before adjournment. These corrective bills will appear in later volumes of this series.)

PAYMENT OF PRODUCTION TAX ON OIL PROVIDED

(Approved October 13, 1933)

H. B. No. 55

CHAPTER 12

Be it enacted by the Legislature of the State of Texas:

SECTION 1. Section 2 of Chapter 162, H. B. No. 154,, Acts of the Forty-third Legislature, Regular Session, is hereby amended so as to hereafter read as follows:

"Sec. 2. (1) There is hereby levied an *occupation tax* on oil produced within this State of two (2) cents per barrel of forty-two (42) standard gallons. Said Tax shall be computed upon the total barrels of oil produced or salvaged from the earth or waters of this State without any deductions, and shall be based upon tank tables showing one hundred percent (100%) of production and exact measurements of contents. Provided however, that the occupation tax herein levied on oil shall be two per cent (2%) of the market value of said oil whenever the market value thereof is in excess of One Dollar ($1.00) per barrel of forty-two (42) standard gallons. The market value of oil, as that term is herein used, shall be

the actual market value thereof, plus any bonus or premium, or other thing of value paid therefor or which such oil does or will reasonably bring, if produced in accordance with the laws, rules and regulations of the State of Texas. (Italics ours).

"(2) The tax hereby levied shall be a liability of the producer of oil and it shall be the duty of such producer to keep accurate records of all oil produced; making monthly reports under oath as hereinafter provided.

"(3) The purchaser of oil shall pay the tax on all oil purchased and deduct tax so paid from payment due producer or other interest holder, making such payments so deducted to the Comptroller of Public Accounts by legal tender or cashier's check payable to the State Treasury.

"Provided, that if oil produced is not sold during the month in which produced, then said producer shall pay the tax at the same rate and in the manner as if said oil were sold.

"(4) The tax herein levied shall be paid monthly on the 25th day of each month on all oil produced during the month next preceeding by the purchaser or the producer as the case may be, but in no event, shall a producer be relieved of responsibility for the tax until same shall have been paid; and provided, in event the amount of the tax herein levied shall be withheld by a purchaser from payments due a producer and said purchaser fails to make payment of the tax to the State as provided herein, the producer may bring legal action against such purchaser to recover the amount of tax so withheld, together with penalties and interest which may have accrued by failure to make payments and shall be entitled to reasonable attorney fees and Court costs incurred by such legal action.

"(5) Provided that unless such payment of tax on all oil produced during any month or fractional part thereof shall be made on or before the 25th of the month immediately following, such payment shall become delinquent and a penalty of ten percent (10%) of the amount of the tax shall be added; such tax and penalty shall bear interest at the rate of six percent (6%) per annum from date due until date paid.

"(6) The tax herein levied shall be borne ratably by all interested parties, including royalty interests; and producers and/or purchaser of oil are hereby authorized and required to withhold from any payment due interested parties, the proportionate tax due.

"(7) The taxes herein provided for, when paid shall be, and hereby are, allocated as follows, to-wit:

"One-half of said tax when and as received by the Comptroller shall be paid to the State Treasurer of Texas and be placed to the credit of the Public School Fund, and one-half of such taxes when and as received by the Comptroller shall be paid to the State Treasurer to be placed to the credit of the General Fund of the State."

SEC. 2. Section 3 of Chapter 162, H. B. No. 154, Acts of the Forty-third Legislature, Regular Session is hereby amended so as to hereafter read as follows:

"Sec. 3.[1] (1) Producers and/or purchasers of oil shall keep in Texas a complete record of all oil produced and a record of all oil sold; reports shall be filed with the Comptroller monthly by producers and purchasers, not later than the 25th of each calendar month, showing the amount of oil produced and the amount of oil sold during the month preceding, upon forms furnished by the Comptroller.

"(2) All railroads, barges, trucks or pipe lines, carrying or transporting oil for hire, for themselves or their owners shall keep in Texas a complete and accurate record of all oil so handled by months, showing date received, number of barrels, by whom received, point of delivery, to whom delivered and manner of transportation and such records shall be open to the inspection of the duly authorized agents of the Comptroller or the Attorney General at all times, and, if requested by the Comptroller, shall furnish information and reports of movements as often as required by the Comptroller."

SEC. 3.[2] Section 5 of Chapter 162, H. B. No. 154, Acts of the Forty-third Legislature, Regular Session, is hereby amended so as to hereafter read as follows:

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1. Amended, infra p. 45.
2. Amended, infra p. 48.

"Sec. 5. (1) Monthly reports by producers shall be filed with the Comptroller upon such forms as may be designated by that official, showing the total number of barrels of oil produced monthly, the name of the county from which produced, the name of the lease from which produced, the disposition made of such oil if sold, the name and correct address of the purchaser, and if not sold, the location of storage, if owned by such operator, or if stored with a pipe line or a refinery, the correct name and address of such pipe line or refinery. All reports so made shall be duly sworn to by the producer or his authorized agent.

"(2) Purchasers of oil shall accompany the remittance for taxes deducted from settlements as provided herein, with a statement or report in a form to be prescribed by the Comptroller, showing complete information requested in such form, including name and address of producer from whom oil was purchased; name of the county from which such oil was produced; name of the lease and the total number of barrels purchased."

SEC. 4. Section 9 of Chapter 162, H. B. No. 154, Acts of the Forty-third Legislature, Regular Session, is hereby amended so as to herafter read, as follows:

"Sec. 9.[1] It shall be the duty of the Comptroller to promulgate rules and regulations governing the detail administration of the terms and requirements of this Act not specifically mentioned herein; to employ auditors or tax supervisors for the purpose of verifying reports and investigating the affairs of producers and/or purchasers to determine whether the tax is being properly reported and paid; to provide the necessary office help and equipment for the proper execution of the provisions of this Act, and for the purpose of defraying the necessary expense of said administration, including salaries of supervisors, auditors, office help, filing equipment, typewriters and supplies, printing of forms, publication of regulations, postage, telephone and telegraph, traveling expenses of employees, and traveling expenses of witnesses not otherwise paid; that the following sums of money, or as much thereof as may be necessary, be and the same are hereby appropriated

1. Amended, infra p. 49.

out of said amount of taxes collected as herein set out for the support and maintenance of the gross production tax division of the Comptroller's office for the two (2) year period beginning September 1, 1933, and ending August 31, 1935.

SEC. 5. The fact that the Forty-third Legislature in enacting said Act failed to provide sufficient time to permit computation and payment of the tax before same becomes delinquent, and the fact that said Forty-third Legislature failed to appropriate sufficient funds for employees in said division sufficient to adequately enforce said Act so that at the present time the Comptroller is hampered in the performance of such duties by insufficient help, create an emergency and an imperative public necessity that the Constitutional Rule that all bills be read on three several days in each House be suspended, and said Rule is hereby suspended, and this Act shall take effect and be in force from and after its passage, and it is so enacted.

OIL TAXES WITH PENALTIES FOR EVASION

(Approved May 30, 1935)

H. B. No. 89

Be it enacted by the Legislature of the State of Texas:

SECTION 1. That Section 1, of Chapter 162, House Bill 154, Acts of the Forty-third Legislature, Regular Session, referred to herein as Chapter 162, is hereby amended so as to hereafter read as follows:

"Section 1. (1). For the purpose of this Act 'producer' shall mean any person owning, controlling, managing or leasing any oil well and/or any person who produces in any manner any oil by taking it from the earth or waters in this State, and shall include any person owning any royalty or other interest in any oil or its value whether produced by him, or by some other person on his behalf, either by lease, contract or otherwise.

"(2). 'First purchaser' shall mean any person purchasing crude oil from the producer.

"(3). 'Subsequent purchaser' shall mean any person operatnig any reclamation plant, topping plant, treating plant, refinery, and/or any kind or character of processing plant, or anyone who purchases oil for any purpose whatsoever, when said oil is purchased from any person other than the producer.

"(4). 'Carrier' shall mean the owner, operator, or manager of any means of transporting oil or any instrumentality that may now be used or come into use.

"(5). 'Oil' shall mean crude oil, or other oil taken from the earth, regardless of gravity of the oil.

"(6). 'Report' shall mean any report required to be furnished in this Act or that may be required by the Comptroller in the administration of this Act.

"(7). 'Person' shall include any person, firm, concern, receiver, trustee, executor, administrator, agent, institution, association, partnership, company corporation, and persons acting under declarations of trust as well as the trustees acting under said declarations of trust.

"(8). 'Production' or 'total oil produced' shall mean the total gross amount of oil produced including all royalty or other interest; that is, the amount for the purpose of the tax imposed by this Article shall be measured or determined by tank tables compiled to show one hundred (100) per cent of the full capacity of tanks without deductions for overage or losses in handling. Allowance for any reasonable and bona fide deduction for basic sediment and water, and for correction of temperature to sixty (60) degrees Fahrenheit will be allowed. If the amount of oil produced has been measured or determined by tank tables complied to show less than one hundred (100) per cent of the full capacity of tanks, then such amount shall be raised to a basis of one hundred (100) per cent for the purpose of the tax imposed by this Article.

"(9). 'Royalty owners' shall mean and include all persons owning any mineral rights under any producing leasehold within this State, other than the working interest, which working interest is that of the person having the management and operation of the well.

"(10). 'Comptroller' shall mean Comptroller of Public Accounts of the State of Texas.

"(11). 'Commission' shall mean the Railroad Commission of Texas.

"(12). The Tax herein imposed on the producing of crude petroleum shall be the primary liability of the producer as hereinbefore defined, and every person purchasing crude petroleum from the producer thereof and taking delivery thereof at the premises where produced shall collect said tax imposed by this Act from the producer. Every purchaser, including the first purchaser and the subsequent purchaser, required to collect any tax under this Act, shall make such collection by deducting and withholding the amount of such tax from any payments made by such purchaser, to the producer, and remit same as herein provided. This Section shall not affect any pending law suit in the State of Texas, or any lease agreement or contract now or that hereafter may be in affect between the State of Texas or any political subdivision thereof and/or The University of Texas and any oil producer.

"(13). When it shall appear that a taxpayer to whom the provisions of this Act shall apply has erroneously paid more taxes than were due during any taxpaying period either on the account of a mistake of fact or law, it shall be the duty of the State Comptroller to credit the total amount of taxes due by such taxpayer for the current period with the total amount of taxes so erroneously paid.

"(14). The tax hereby levied shall be a liability upon the producer, the first purchaser, and/or subsequent purchaser or purchasers as herein provided.

"(15). The tax hereby levied shall be paid by the first purchaser purchasing the same from the producer, who shall deduct the same from the amount paid producer, as aforesaid, provided, however, that the failure of first purchaser to pay said tax shall not relieve the producer from the payment of same, nor shall it relieve any subsequent purchaser from the payment of same, where the first purchaser does not account for and pay said tax, and the State shall have a lien on all of the oil produced in Texas in the hands of the producer, the

first purchaser and any subsequent purchaser to secure the payment of the tax due, and it shall be the duty of every person purchasing oil produced in Texas to satisfy himself or itself that the tax on said oil has been or will be paid by the persons primarily liable therefor.

"(16). If the oil produced by said producer is not sold during the month in which it is produced, then said producer shall pay the tax at the same rate and in the same manner as if said oil were sold during said month. In such case, however, the working interest operator may pay such tax and deduct it from the interest of the other interest holders."

SEC. 2. Section 3 of said Chapter 162, as amended by House Bill 55, Chapter 12, Acts of the First Called Session of the Forty-third Legislature be and the same is hereby amended so as to hereafter read as follows:

"Section 3. (1). A complete record shall be kept by every producer of oil within this State, said records to show the county or counties in which said producer operates, the correct name or names of the lease or leases from which oil is produced, the total number of barrels of oil produced from each lease, the correct name and address of the first purchaser, the total number of barrels of oil sold or delivered to each first purchaser and the price received therefor. And in addition shall keep a record of all oil used on the lease from which said oil is produced or which may be refined or processed in any manner by the producer upon the lease from which said oil is produced; and if said oil is not sold, the location of storage and the total number of barrels in storage, if owned by such operator, or if stored with a pipe line or a refinery, the correct name and address of such pipe line or refinery.

"(2). Every producer shall file monthly on the 25th day of each month with the Comptroller under oath of the producer or his duly authorized agent a report showing the total number of barrels of oil produced by said producer during the month preceding the date of the report, the county in which the oil is produced, the correct name of the lease from which the oil is produced, the correct name and address of the first

purchaser of said oil and the price received therefor, and such other information as Comptroller may require; said records and reports shall be open to the inspection of the Comptroller or the Attorney General or the duly authorized agents of the Comptroller or Attorney General.

"(3). Every first purchaser shall keep in Texas records showing the correct name and address of the producer from whom said first purchaser buys oil, the county in which said oil is produced, the true and correct name of the lease from which said oil is produced, the total number of barrels bought, and the price paid therefor; and in addition shall keep a record showing the total number of barrels of said oil purchased and used, refined, or processed in any manner by said first purchaser and the total number of barrels of oil sold by him, the price received therefor, and the true and correct name and address of the subsequent purchaser of said oil. On the 25th day of each month each and every first purchaser of oil shall file with the Comptroller, under oath of the first purchaser or his duly authorized agent, a report showing the total number of barrels of oil purchased during the preceding month, the price paid therefor, the correct name and address of the producer or producers from whom said oil purchased, the county in which the oil was produced, and the correct name of the lease from which said oil was produced, and such other information as Comptroller may require; said records and reports shall be open to the inspection of the Comptroller and/or Attorney General or their duly authorized agents.

"(4.) Each and every subsequent purchaser, shall keep in Texas a record showing the correct name and address of each first purchaser or subsequent purchaser from whom any oil is bought, the total number of barrels purchased and the price paid therefor, the date of purchase, the disposition of said oil, the total number of barrels used, refined, or processed in any manner by said subsequent purchaser, and if sold shall show the correct name and address of the subsequent purchaser to whom said oil is sold or delivered and the date of said sale and/or delivery, and the price received therefor.

"(5) Each and every subsequent purchaser shall file with the Comptroller on the 25th day of each month a report under

oath of the subsequent purchaser or a duly authorized agent showing the correct name and address of the person from whom said subsequent purchaser has bought oil during the preceding month, the total number of barrels purchased, the price paid therefor, and the disposition of said oil; said reports to show the total number of barrels of oil used, refined, or processed in any manner by said subsequent purchaser and the correct name and address of any subsequent purchaser to whom said oil was sold and the number of barrels sold, and the price received therefor; said records and reports shall be open to the inspection of the Comptroller or the Attorney General or the duly authorized agents of the Comptroller or Attorney General.

"(6) Royalty owners shall only keep a record of all moneys received as royalty from any producing leasehold within this State. They shall also keep a copy of all settlement sheets furnished them by the purchaser or operator or any other statement showing the number of barrels of oil from which royalty was received and the amount of tax deducted; said records shall be open to the inspection of the Comptroller or the Attorney General or their duly authorized agents.

"(7) Every carrier, including all railroads, barges, trucks, or pipe lines, carrying or transporting oil for hire, for themselves or their owners, shall keep in Texas a complete and accurate record of all oil so handled by months, showing date received, number of barrels, of whom received, point of delivery, to whom delivered and manner of transportation, and such records shall be open to the inspection of the duly authorized agents of the Comptroller or the Attorney General at all times, and, if requested by the Comptroller, shall furnish information and reports of movements as often as required by the Comptroller; provided however, that nothing in this bill imposing a tax on those enjoying the privilege herein taxed shall be construed as impairing any contract whereby any interest holder or other person has agreed to pay any part of the tax in the past or in the future, but said tax is imposed on all of said interest holders as their interests appear and shall be paid as herein provided, and this Act is not

intended to relieve any person of any contractual liability whatsoever."

SEC. 3. That Section 5 of said Chapter 162, as amended by House Bill 55, Chapter 12, Acts of the First Called Session of the Forty-third Legislature, be and the same is hereby amended so as to hereafter read as follows:

"Section 5. (1) At the time of filing the reports herein required, the first purchaser shall pay to the Comptroller by legal tender or cashier's check, payable to the State Treasurer, the tax herein required to be paid. Failure to pay said tax on the twenty-fifth day of the month immediately following, shall cause said tax to become delinquent and a penalty of ten (10) per cent of the amount of said tax shall be added, such tax and penalty to bear interest at the rate of six (6) per cent per annum from the date due until the date paid."

SEC. 4. That Section 6 of said Chapter 162 be and the same is hereby amended so as to hereafter read as follows:

"Section 6. (1) For the tax, penalties and interest herein provided for, the State shall have a prior and preferred lien on every leasehold interest, ownership of the oil rights, or the value of oil rights or other interest, including oil produced and oil runs owned by the person owing any tax herein, and in addition thereto such lien shall include equipment, tools, tanks, and all other implements used on said lease from which oil is produced. Said lien shall extend to and be enforceable against any property, either real or personal, or both, owned by any person or persons made liable for the tax herein levied, which property is not exempt from forced sale by reason of existing laws or the Constitution of this State. It is further provided that when any oil is discovered upon which the tax herein provided for has not been paid as and when provided for herein, any sheriff, ranger or other peace officer is authorized to levy on said oil by notice to the owner or other person in charge, that said oil is levied on for taxes due on it and after ten (10) days notice posted at the site of the oil, said officer shall proceed to sell said oil to the highest bidder for cash. Any money received for said oil in excess of the taxes and ten (10) per

cent commission to the officer selling the property, shall be paid by said officer to the owner of said oil. The officer selling same shall transmit the amount of the tax to the Comptroller or his duly authorized representative. Should the oil sold fail to sell for enough to pay said taxes, the officer selling same shall deduct ten (10) per cent of the amount received and forward the balance to the Comptroller. Provided however, that no ranger shall receive any commission for services performed in the enforcement of this provision."

SEC. 5. That Section 8 of said Chapter 162 be and the same is hereby amended so as to hereafter read as follows:

"Section 8. Whoever, as producer, first purchaser, subsequent purchaser, or carrier, or whoever shall as a principal or as agent or representative of such principal, knowingly make any false entries or fail to make any proper entries in the books required by this Act with intent to defraud the State; or whoever as such, shall knowingly make a false or incomplete report as required by this Act; or whoever, as such, shall knowingly fail or refuse to make the report required to be made; or whoever, as such, shall destroy, mutilate, or secrete any of the records required to be kept by the provisions of this Act; or whoever shall, as such, hide or secrete with intent to defraud, any of the property upon which a lien is created hereunder, or whoever fails or refuses to permit the Comptroller or the Attorney General or the duly authorized representative of either to inspect the records and reports herein provided for, shall be guilty of a misdemeanor and upon conviction thereof shall be fined in the sum of not less than Twenty-five Dollars ($25), nor more than Five Thousand Dollars ($5,000) or confined in the county jail for not less than one month, nor more than six (6) months, or by both such fine and imprisonment."

SEC. 6. That Section 9, Chapter 162, H. B. 154, Acts of the Regular Session of the Forty-third Legislature, as amended by Chapter 12, H. B. 55, First Called Session of the Forty-third Legislature, be and the same is hereby amended so as to hereafter read as follows:

"Section 9. (1). It shall be the duty of the Comptroller to promulgate rules and regulations governing the detail administration of the terms and requirements of this Act not specifically mentioned herein; to employ auditors and supervisors for the purpose of verifying reports and investigating the affairs of producers and/or purchasers to determine whether the tax is being properly reported and paid. Before any division or allotment of the occupation tax on oil collected under the provisions of this Act, is made one-half of one per cent of the gross amount of said tax shall be set aside in the Treasury subject to the use of the Comptroller in the administration and enforcement of the provisions of this Act, and so much of the said proceeds of one-half of one per cent of the occupation tax on oil paid monthly as may be needed in such administration and enforcement shall be expended in the amounts and for the purposes fixed by the Legislature in the General Appropriation Bill. Any unexpended portion of said fund so specified shall at the end of the fiscal year revert to the respective funds or accounts in proper proportions to which the occupation tax on oil is proportioned at the end of the fiscal year; and provided that the Comptroller may appoint only six (6) additional supervisors or auditors. No salary to exceed those set out in the Department Appropriation Bill, for places of the same type of service.

"(2). Provided that said appropriation herein provided for shall include as a part of said one-half of one per cent of the said tax herein appropriated the appropriation made by the Regular Session of the Forty-third Legislature for said Comptroller's Department for the purpose herein mentioned."

SEC. 7. If any clause, section, provision or portion of this Act shall be held to be invalid or unconstitutional, such holding shall not affect any other section or clause of this Act.

SEC. 8. The fact that under existing Statutes the State is losing large sums of money by enormous tax evasions due to the ambiguity and inadequacies of said Act, the fact that by the passage of this bill the Comptroller will be able to ferret out such evasions and enforce the payment of taxes due the State, and said tax will be more uniform, create an emergency

and an impertive public necessity that the Constitutional Rule that all bills be read on three several days in each House be suspended, and said Rule is hereby suspended and this Act shall take effect and be in force from and after its passage, and it is so enacted.

Approved May 30, 1935.
Effective May 30, 1935.

(NOTE: H. B. No. 89 passed the House by a vote of 104 yeas, 2 nays; the Senate by 27 yeas, 1 nay.)

APPENDIX "B"

Vernon's Annotated Texas Statutes Art. 7071

1. Each person owning, controlling, managing, operating or leasing in this State any oil well, or any person who produces in any other manner any oil by taking it from the earth in this State, shall make quarterly on the first days of January, April, July and October of each year, a report to the Comptroller, under oath of such person or if the producer is other than a natural person, under oath of the president, treasurer, superintendent or person in charge of such production, showing the total amount of oil produced by such person from each well, or otherwise, during the quarter next preceding and the average market value thereof during said quarter. Each such person on said first days of January, April, July, and October shall pay to the Treasurer of this State an occupation tax for the quarter beginning on said date equal to two per cent of the value of the total amount of oil produced in this State by such person during the quarter next proceding such first days of January, April, July and October at the average market value thereof.

2. Each person mentioned and included in subdivision 1 of this article shall make, keep and preserve a full and complete record of all such oil produced in this State during the time so engaged in its production, and said record shall be open at all times to the inspection of all tax officers of this State. Any person failing to comply with this requirement

shall be subject to a penalty not less than five hundred and not more than fifteen hundred dollars payable to the State of Texas, and such penalty shall accrue for each ten days of failure to comply with this subdivision of said article and such penalty shall accrue for failure to comply with this subdivision with reference to each separate oil well.

3. In each report required to be made by this article such person making the same shall show in detail the disposition made of any such oil, if disposed of, and if not, shall show where it is stored. Said report shall show to whom any such oil was sold or delivered, the date of sale and delivery, the amount delivered to each, and shall show the name and location of the person, refinery, pipe line, establishment, plant, factory, railroad, institution or place to which or to whom delivery was made.

4. The word "person" as used in this article shall include any person, firm, concern, receiver, receivers, trustee, executor, administrator, agent, institution, association, partnership, company corporations, and persons acting under declarations of trust as well as the trustees acting under such declarations of trust.

5. The market value of oil as that term is used herein shall be the actual market value of the same, and among other things proper to be considered any bonus or premium paid or which the oil will reasonably bring shall not be excluded in arriving at the market value.

6. Any person failing to make proper and accurate report for thirty days from the date when said report is required herein to be made shall forfeit and pay to the State of Texas a penalty of ten per cent of the amount of the tax due for the quarter for which said report is required by law to be made.

7. Any person failing to pay any tax provided for herein within thirty days from the date when said tax is required herein to be paid shall forfeit and pay to the State of Texas a penalty of ten per cent upon the amount of such tax and six per cent interest upon the amount of such tax/and penalty from date when due and payable until paid.

8. The word "oil" as used in this law means petroleum oil, mineral oil, or other oil taken from the earth.

9. For the occupation tax, penalties and interest herein provided for, the State shall have a lien on any leasehold interest, ownership of the oil rights or interest owned by the person owing any tax herein provided for. (Acts 1907, p. 479; Acts 1919, p. 128; Acts 1923, 2nd C .S., p. 98).

APPENDIX "C"

CONSTITUTION OF TEXAS

(From Vernon's Annotated Texas Statutes "Constitution" - Vol. 2, pp. 476-503)

ARTICLE VIII.

SECTION 1. *Taxation shall be equal and uniform. All property in this State, whether owned by natural persons or corporations, other than municipal, shall be taxed in proportion to its value, which shall be ascertained as may be provided by law.* The Legislature may impose a poll tax. It may also impose *occupation taxes,* both upon natural persons and upon corporations, other than municipal, doing any business in this State. It may also tax incomes of both natural persons and corporations other than municipal, except that persons engaged in mechanical and agricultural pursuits shall never be required to pay an occupation tax. * * * * (Italics ours).

SECTION 2. All Occupation taxes shall be equal and uniform upon the same class of subjects within the limits of the authority levying the tax. * * * *.

SECTION 9. *The State tax on property, exclusive of the tax necessary to pay the public debt, and of the taxes provided for the benefit of the public free schools, shall never exceed thirty-five cents on the one hundred dollars valuation;* and no county, city or town shall levy more than twenty-five cents for city or county purposes, and not exceeding fifteen cents for roads and bridges, and not exceeding fifteen cents to pay jurors, on the one hundred dollars valuation. * * * *.

SECTION 11. *All property, whether owned by persons or corporations shall be assessed for taxation, and the taxes paid in the county where situated,* but the Legislature may, by a two-thirds vote, authorize the payment of taxes of non-residents of counties to be made at the office of the Comptroller of Public Accounts. And all lands and other property not rendered for taxation by the owner thereof shall be assessed at its fair value by the proper officer. * * * *

SEC. 18. *The Legislature shall provide for equalizing, as near as may be, the valuation of all property subject to or rendered for taxation,* (*The County Commissioners' Court to constitute a board of equalization*); and may also provide for the classification of all lands with reference to their value in the several counties.

SHEFFIELD vs. HOGG, 77 S. W. (2d) 1021, 1024, (Tex. Sup.) Decided December 31, 1934

Holds, that *a lessor's reserved royalty interest* in an oil and gas lease, in whatever form the reservation is made *is "an interest in land, subject to taxation* as such *in the counties in which the respective tracts of land are situated."*

And, in the same case (p. 1030) it is said that: "Under the contract, *the lessees having to pay all expenses of exploration and production,* each one-eighth out of their seven-eighth mineral interest was necessarily worth less than the one-eighth interest of the lessor."

NOTE: It was because of these Constitutional limitations upon the taxing power, that appellants believe the Court of Civil Appeals held that its construction of the law in question as an occupation tax on those interested in the oil produced in proportion to their respective interests therein, was "required to save it from the vice of unconstitutionality." (R. 50.)

APPENDIX "D"

Vernon's Annotated Texas Statutes (Supp.) Art. 7057-B

(Acts 1933, 43rd Legislature, page 637, Chapter 214)

(Art. 7057-b. *Payment of License or Privilege Taxes Under Protest*)

SEC. 1. Any person, firm or corporation who may be required to pay to the head of any department of the State Government any occupation, gross receipt, franchise, license or other privilege tax or fee, and who believes or contends that the same is unlawful and that such public official is not lawfully entitled to demand or collect the same shall, nevertheless, be required to pay such amount as such public official charged with the collection thereof may deem to be due the State, and shall be entitled to accompany such payment with a written protest, setting out fully and in detail each and every ground or reason why it is contended that such demand is unlawful or unauthorized.

(*Suits for Recovery of Taxes or Fees*)

SECTION 2. Upon the payment of such taxes or fees, accompanied by such written protest, the taxpayer shall have ninety (90) days from said date within which to file suit for the recovery thereof in any court of competent jurisdiction in Travis County, Texas, and none other. Such suit shall be brought against the public officials charged with the duty of collecting such tax or fees, the State Treasurer and the Attorney General. The issues to be determined in such suit shall be only those arising out of the grounds or reasons set forth in such written protest as originally filed. The right of appeal shall exist as in other cases provided by law. Provided, however, where a class action is brought by any taxpayer all other taxpayers belonging to the class and represented in such class action who have properly protested as herein provided shall not be required to file separate suits but shall be entitled to and goverened by the decision rendered in such class action.

(*Lists Remitted to State Treasurer.*)

SEC. 3. It shall be the duty of such public official to

transmit daily to the State Treasurer all money so received, with a detailed list of all those remitting same, and he shall inform the State Treasurer in writing that such money was paid under protest as hereinabove provided. A deposit receipt shall be issued by the Comptroller for the daily total of such remittances from each department; and the cashier of the Treasury Department shall keep a cash book to be called "Suspense Cash Book," in which to enter such deposit receipts. Upon the receipt of such money by the State Treasurer it shall be his duty and he is hereby required to immediately and forthwith place the same in State depositories bearing interest in the same manner as any other funds of the State required to be placed in such depositories at interest, and the State Treasurer shall further be required to allocate whatever interest is earned on such funds and to credit the amount thereof to such suspense account until the status of such money is finally determined as herein provided.

APPENDIX "E"

(Cases listed alphabetically)

APPLEBY v. NEW YORK, 271 U. S. 364:

"The questions we have here to determine are, first, was there a contract; second, what was its proper construction and effect, and third was its obligation impaired by subsequent legislation as enforced by the state court? These questions we must answer independently of the conclusion of that court. Of course we should give all proper weight to its judgment, but we cannot perform our duty to enforce the guaranty of the Federal Constitution as to the inviolability of contracts by state legislative action, unless we give the questions independent consideration. It makes no difference what the answer to them involves, whether it turns on issues of general or purely local law, we cannot surrender the duty to exercise our own judgment. In the case before us, the construction and effect of the contract involved in the deeds and covenants depended chiefly upon the extent of the power of the State and city to part with property under navigable waters to private persons, free from subsequent regulatory control of the water over the land and the land itself. That is a State question, and we must determine it from the law of the State, as it was when the deeds were executed, to be derived from statutes then in force and from the decisions of the courts then and since made, but we must give our own judgment derived from such sources and not accept the present conclusion of the State court without inquiry."

BLACK & WHITE TAXICAB & TRANSFER CO. v. BROWN & YELLOW TAXICAB & TRANSFER CO., 276 U. S. 518.

"The decree below should be affirmed unless Federal courts are bound by Kentucky decisions which are directly opposed to this court's determination of the principles of common law properly to be applied in such cases. Petitioner argues that the Kentucky decisions are persuasive and establish the invalidity of such contracts and that the Circuit Court of Ap-

peals erred in refusing to follow them. But, as we understand the brief, it does not contend that, by reason of the rule of decision declared by Sec. 34 of the Judiciary Act of 1789 (now Rev. Stat. Sec. 721, U. S. C. title 28, Sec. 725), this court is required to adopt the Kentucky decisions. But, granting that this point is before us, it cannot be sustained. The contract gives respondent, subject to termination on short notice, license or privilege to solicit patronage and park its vehicles on railroad property at train time. There is no question concerning title to land. No provision of State statute or constitution and no ancient or fixed local usage is involved. For the discovery of common law principles applicable in any case, investigation is not limited to the decisions of the courts of the State in which the controversy arises. State and Federal courts go to the same sources for evidence of the existing applicable rule. The effort of both is to ascertain that rule. Kentucky has adopted the common law and her courts recognize that its principles are not local but are included in the body of law constituting the general jurisprudence prevailing wherever the common law is recognized. As respects the rule of decision to be followed by Federal courts, distinction has always been made between statutes of a State and the decisions of its courts on questions of general law. The applicable rule sustained by many decisions of this court is that in determining questions of general law, Federal courts, while inclining to follow the decisions of the courts of the State in which the controversy arises, are free to exercise their own independent judgment. That this case depends on such a question is clearly shown by many decisions of this court. *Swift v. Tyson*, 16 Pet. 1, was an action on a bill of exchange. Mr. Justice Story, writing for the court, fully expounded Sec. 34 of the Judiciary Act. *Carpenter v. Providence Washington Ins. Co.* 16 Pet. 495, held that the construction of an insurance policy involves questions of general law. *Lane v. Vick*, 3 How. 464, involved the construction of a will. It was said: "This court do not follow the State courts in their construction of a will or any other instrument, as they do in the construction of satutes." *Foxcroft v. Mallett*, 4 How. 353, held that the decision of a State court construing

a deed is not conclusive on this court. *Chicago v. Robbins*, 2 Black, 418, declined to follow the determination of the State court as to what constitutes negligence. *Yates v. Milwaukee*, 10 Wall. 497, held that the determination of what constitutes a dedication of land to public use is one of general law. *Olcott v. Fon du Lac County*, 16 Wall. 678, held that the determination of what is a public purpose to warrant municipal taxation involves a question of general law. *New York C. R. Co. v. Lockwood*, 17 Wall. 357, declined to follow the State rule as to liability of common carriers for injury of passengers. *Liverpool & G. W. Steam Co. v. Phenix Ins. Co.*, 129 U. S. 397, held a question concerning the validity of a contract for carriage of goods is one of general law. *Baltimore & O. R. Co. v. Baugh*, 149 U. S. 368, so held as to the responsibility of a railroad company to its employees for personal injuries. *Beutler v. Grand Trunk Junction R. Co.*, 224 U. S. 85, decides who are fellow servants as a question of general law."

COLUMBIA RAILWAY, GAS, & ELECTRIC CO. *v.* STATE OF SOUTH CAROLINA, 261 U. S. 236.

"But, although the State court may have construed the contract and placed its decision distinctly upon its own construction, if it appear, upon examination, that, in real substance and effect, force has been given to the statute complained of, our jurisdiction attaches. In *Houston & T. C. R. Co. v. Texas*, 177 U. S. 66, this court said:

" 'Thus we see that although the decision of the State court was based upon the ground that the warrants in which these payments were made had been issued in utter violation of the State Constitution, and were hence void, and that no payments made with such warrants had any validity, and although this ground of invalidity was arrived at without any reference made to the Act of 1870, yet the necessary consequence of the judgment was that effect was thereby given to that Act, and in a manner which the company has always claimed to be illegal and unwarranted by the Act when properly construed. The company has never accepted such a con-

struction, but, on the contrary, has always opposed it, and raises the question in this proceeding at the very outset. Upon these facts this court has jurisdiction, and it is its duty to determine for itself the existence, construction, and validity of the alleged contract, and also to determine whether, as construed by this court, it has been impaired by any subsequent State legislation to which effect has been given by the court below.'"

CRESWILL v. GRAND LODGE K. OF P., 225 U. S. 246, 261.

"While it is true that upon a writ of error to a State court we do not review findings of fact, nevertheless two propositions are as well settled as the rule itself, as follows: (a) that where a Federal right has been denied as the result of a finding of fact which it is contended there was no evidence whatever to support and the evidence is in the record, the resulting question of law is open for decision; and (b) that where a conclusion of law as to a Federal right and a finding of fact are so intermingled as to cause it to be essentially necessary, for the purpose of passing upon the Federal question, to analyze and dissect the facts, to the extent necessary to do so the power exists as a necessary incident to a decision upon the claim of denial of the Federal right."

DAWSON *v.* KENTUCKY DISTILLERIES & WAREHOUSE COMPANY, 255 U. S. 288.

This case involved the constitutionality of a tax upon all persons engaged in the business of manufacturing, *owning and storing* whisky, or "in the *business of owning* and storing" the same in bonded warehouses within the State, called an "annual license tax" of 50c a gallon upon "all whisky withdrawn from bond or transferred in bond from Kentucky to a point outside the State." The right to withdrawn whisky was evidenced by the negotiable warehouse receipts. The warehouseman was required to collect the tax and pay it to the State. The court said:

"The thing really taxed is the act of the owner in taking his

property out of storage into his own possession, for the purpose of making some one of the only uses of which it is capable. * * * The whole value of the whisky depends upon the owner's right to get it from the place where the law has compelled him to put it, and to tax the right is to tax the value." "To levy a tax by reason of ownership of property is to tax the property. * * * It cannot be made an occupation or license tax by calling it so."

Here we have illustrated a tax upon *a right in property*, held to be the same as a tax upon the property itself. The exercise of the right to withdraw the liquor, was held to be a property right indistinguishable from the right *to* the liquor itself.

EDUCATIONAL FILMS CORPORATION v. WARD,
282 U. S. 379, 387-388.

"But the nature of a tax must be determined by its operation rather than by particular descriptive language which may have been applied to it. As was said in *Macallen Co. v. Massachusetts*, 279 U. S. 620, 625, 626, 'neither State courts nor legislatures, by giving the tax a particular name, or by using some form of words, can take away our duty to consider its nature and effect. This court must determine for itself by independent inquiry whether the tax here is what in form and by the decision of the State court it is declared to be.' On appeal from the State court in *People ex rel. Bass, Ratcliff & Gretton v. Tax Commission*, 232 N. Y. 43, 46, 133 N. E. 122, this court upheld the tax and defined its nature, saying, 266 U. S. 271, 280, 'It is not a direct tax upon the allocated income of the corporation in a given year, but a tax for the privilege of doing business in one year measured by the allocated income accruing from the business in the preceding year.'"

FLINT v. STONE TRACY COMPANY, 220 U. S. 107, —

And the cases decided with it, involved the constitutionality of the act of Congress which made *every corporation engaged*

in business subject to a special excise tax "with respect to the carrying on, or doing business by such corporation," of 1% of its net income. (Id. 143 to 145). The corporations contend that, in the light of the Pollock case, the so-called excise tax was nothing but a tax upon their property. Pointing to the fact that the law expressly declared, and the circumstances showed, that besides their physical properties and the income thereof the corporations to be subject to the tax must be and most of them were possessed of a going concern value the court said:

"It is therefore apparent, giving all of the words of the statute effect, that the tax is imposed not * * * * upon the property of the corporation, but upon the doing of corporate * * * * business, and with respect to the carrying on thereof." "In other words the tax is imposed upon the doing of business of the character described, and the measure *of the tax is to be the income.*" * * * *

The court reiterated the view expressed in the Pollock case that "an act might lay a direct tax on real or personal property, and at the same time also lay excise taxes on business, privileges, employments and vocations."

The court further said:

"Within the category of indirect taxation * * * * is embraced a tax upon business done in a corporate capacity, which is the subject matter of the tax imposed in the act under consideration. The Pollock case construed the tax there levied as direct, because it was imposed upon property simply because of its ownership. In the present case *the tax is not payable, unless there be carrying on or doing of business in the designated capacity, and this is made the occasion for the tax,* measured by the standard prescribed. THE DIFFERENCE BETWEEN THE ACTS IS NOT MERELY NOMINAL, *BUT RESTS UPON* SUBSTANTIAL *DIFFERENCES* BETWEEN THE *MERE OWNNERSHIP* OF PROPERTY *AND* THE *ACTIVE DOING OF BUSINESS* IN A CERTAIN WAY. The tax, as we have construed the statute may be described as an excise upon the particular privilege of doing business in a corporate capacity, i. e., with the advan-

tages which arise from corporate or quasi-corporate organizations; * * * * *the requirement to pay such taxes involves the exercise of privileges, and the element of absolute and unavoidable demand is lacking.* If business is not done in the manner described in the statute, no tax is payable (Id. 151, 152)."

Referring to the fact that the method of measuring a tax—apportioning it—is often confused with the character and nature of the tax itself *G. H. & S. A. Railway Co. v. Texas,* 210 U. S. 217, supra, is cited as involving an attempt to directly tax receipts of a carrier from interstate commerce. The fact that the tax was measured by an amount of 1%, or equal to 1%, is shown to be of no consequence. *Western Union Telegraph Company v. Kansas,* 216 U. S. 1, was cited as holding that a charter fee based upon the entire capital of a company engaged in interstate commerce was in reality a tax upon such commerce, and a tax on property beyond the jurisdiction of the State. The court observed:

"There is nothing in these cases contrary * * * * to the familiar rulings of this court which hold that WHERE A TAX IS LAWFULLY IMPOSED UPON THE EXERCISE OF PRIVILEGES * * * * THE MEASURE OF SUCH TAX MAY BE THE INCOME FROM THE PROPERTY OF THE CORPORATION. * * * * *The distinction lies between an attempt to tax the property as such, and to measure a legitimate tax upon the privileges enjoyed in the use of such property.*"

In the couse of the decision, it became necessary to determine whether certain corporations, parties to the litigation, were *doing business* within the meaning of the law. It was held that corporations organized to lease properties, collect rentals, manage office buildings, make investments, lease land, collect royalties, manage wharves, and in some cases reinvest the surplus, were engaged in business within the meaning of the law.

FOX RIVER PAPER COMPANY v. RAILROAD COMMISSION, 274 U. S., 651.

"There being no question of evasion of the constitutional issue, this court on writ of error must accept as final the ruling of the state court of last resort on all matters of state law. * * * * We accept as conclusive the state court's view of the nature of the rights of riparian owners."

FROST v. RAILROAD COMMISSION, 271 U. S. 583.

"That consistently with the due process clause of the 14th amendment, a private carrier cannot be converted against his will into a common carrier by mere legislative command, is a rule not open to doubt."

G. H. & S. A. RY. CO. v. TEXAS, 210 U. S. 217.

The physical properties of Railroad Companies had long been taxed in Texas in the Constitutional[1] method when the Legislature enacted that all Railroad Companies owning and operating railroads should pay a tax "equal to" 1% of their gross receipts. It was contended by the State that this was but an occupation tax. The Railroad Companies argued that the tax was a tax upon their gross receipts, and even if considered as an occupation tax, it taxed receipts from interstate business in violation of the Interstate Commerce clause of the Federal Constitution.

The Supreme Court of Texas held, 97 S. W. 71, that the the tax was levied on the railroads for the privilege of carrying on business in the state, and that it was not a tax upon interstate transactions of the Railroad Company.

This Court reversed the decision and pointing out that neither form nor evasion would prevent the court from considering substance, it held the tax was upon all property of the railroads, both in, and out of the state; that the property and its income were to be considered as one and the same

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1. See Appendix C hereto.

thing; the *"going concern value" was another thing*, that each was subject to separate taxation by the State, but the right to levy on either was limited to the boundaries of the state.

LAWRENCE v. STATE TAX COMMISSION, 286 U. S. 276, 280.

"The present tax has been defined by the Supreme Court of Mississippi as an excise and not a property tax * * * but in passing on its constitutionality we are concerned only with its practical operation, not its definition or the precise form of descriptive words which may be applied to it.

MCCOACH v. MINEHILL S. & H. R. CO., 228 U. S. 295.

A railway company which had constructed and was operating a line of railroad, pursuant to Legislative authority, leased its entire assets to another road for an annual rental and thereafter ceased to do any railway business. It did however, maintain a skeleton organization for the purpose of collecting rentals; it annually elected officers, received the rentals, deposited it, paid the necessary expenses of its office, maintained a contingent fund from which it paid dividends, etc.

The Court held that the company was not liable for the payment of the corporation excise tax involved in *Flint v. Stone Tracy Co.*, saying:

"It is therefore apparent, giving all the words of the statute effect, that the tax is imposed not upon the franchises of the corporation irrespective of their use in business, nor upon the property of the corporation, but upon the doing of corporate or insurance business, and with respect to the carrying on thereof, in the sum equivalent to 2 per centum upon the entire net income over and above $5,000, received from all sources during the year; that is, when imposed in this manner it is a tax upon the doing of business with the advantages which inhere in the peculiarities of corporate or joint stock organizations of the character described. As the latter organizations share many benefits of corporate organization it

may be described generally as a tax upon the doing of business in a corporate capacity. . . . The income is not limited to such as is received from property used in the business, strictly speaking, but is expressly declared to be upon the entire net income above $5,000, from all sources, excluding the amounts received as dividends on stock in other corporations, joint stock companies or associations, or insurance companies also subject to the tax. In other words, the tax is imposed upon the doing of business of the character described, and the measure of the tax is to be the income, with the deduction stated, received not only from property used in business, but from every source. * * *

"The precise question presented by the present record is whether the Minehill Company is 'doing business' in the sense in which the realty companies concerned in *Flint v. Stone Tracy Co.*, 220 U. S. 107, 170, were doing business, or had gone out of business in substantially the same sense that the Minneapolis Syndicate had done so.

"From the facts as stated above it is entirely clear that the Minehill Company was not, during the years of 1909 and 1910 engaged at all in the business of maintaining or operating a railroad, which was the prime object of its incorporation. This business, by the lease of 1896, it had turned over to the Reading Company. If that lease had been made without authorization of law, it may be that for some purposes, and possibly for the present purpose, the lessee might be deemed in law the agent of the lessor; or, at least, the lessor held estopped to deny such agency. But the lease was made by the express authority of the state that created the Minehill Company, conferred upon it its franchise, and imposed upon it the correlative public duties. The effect of this legislation and of the lease made thereunder was to constitute the Reading Company the public agent for operation of the railroad, and to prevent the Minehill Company from carrying on business in respect of the maintenance and operation of the railroad so long as the lease shall continue. And it is the Reading Company, and not the Minehill Company, that is 'doing business' as a railroad company upon the lines covered by the lease, and is taxable because of it."

MICHIGAN PUBLIC UTILITIES COM. v. DUKE, 266 U. S. 570.

Plaintiff was a private carrier, but the law attacked authorized the commission to impose on him the burdens of a common carrier. The court said:

"It is beyond the power of the State by legislative fiat to convert property used exclusively in the business of a private carrier into a public utility, or to make the owner a public carrier, for that would be taking private property for public use without just compensation which no State can do consistently with the due process of law clause of the 14th Amendment."

MURRAY V. CHARLESTON, 96 U. S. 432.

"The city ordinances were in question on the ground of their repugnancy to the inhibition upon the States to make any law impairing the obligation of contracts; and the decision was in favor of their validity. Nothing else was presented for decision, unless it be the question whether the Acts of the State Legislature authorized the ordinances; and that was ruled affirmatively. The jurisdiction of this court over the judgments of the highest courts of the States is not to be avoided by the mere absence of express reference to some provision of the Federal Constitution. Wherever rights acknowledge and protected by that instrument are denied or invaded, under the shield of State legislation, this court is authorized to interfere. The form and mode in which the Federal question is raised in the State court is of minor importance, if, in fact, it was raised and decided."

NEW STATE ICE CO. V. LEIBMANN, 285 U. S. 262.

An Oklahoma law declared the ice business was a public one, and prohibited everyone from engaging therein without securing a license. This court examined fully the ground of the legislative declaration, held that on the facts the business was not affected with a public interest, in the sense of the regulation, and that the statute was void. Even the dissenting opinion admitted that "a legislature cannot by mere legislative fiat convert a business into a public utility."

PRODUCERS TRANSPORTATION CO. v. RAILROAD COMMISSION, 251 U. S. 228.

"It is, of course, true that if the pipe line was constructed solely to carry oil for particular producers under strictly private contracts, and never was devoted by its owner to public use, that is, to carrying for the public, the State could not, by mere legislative fiat or by any regulating order of a commission, convert it into a public utility or make its owner a common carrier."

SCHLESINGER v. WISCONSIN, 270 U. S. 230.

A State law as interpreted made all gifts within six years, gifts in anticipation of death, without regard to the fact of intent. This court said:

"Gifts inter vivos within six years of death, but in fact made without contemplation thereof, are first conclusively presumed to have been so made without regard to actualities, while like gifts at other times are not thus treated. There is no adequate basis for this distinction."

SMITH v. CAHOON, 283 U. S. 553.

A State statute declared all carriers for hire upon public highways were subject to regulation as common carriers, and required a certificate of public necessity and convenience for their operation. Appellant, a private contract carrier, was arrested and sought release on habeas corpus which the State court denied, upholding the validity of the law under the Federal Constitution. This court in reversing the decision, said:

"It is true that the statute does not in express terms demand that a private carrier shall constitute itself a common carrier, but the statute purports to subject all the carriers which are within the terms of its definition to the same obligations. Such a scheme of regulation of the business of a private carrier, such as the appellant, is manifestly beyond the power of the State."

SWISS OIL CORPORATION v. SHANKS, 273 U. S. 407.

This case involved the validity, under the Federal Constitution, of a law of Kentucky levying a gross production tax on producers of oil. The State court held the statute was not violative of the Federal Constitution; that even if the challenged enactment was invalid, the same tax would be due under the prior law.

"As the case is brought here from a State court, the construction put by the court upon the statutes and Constitution of its own State is not open to review here."

TYSON & BRO. v. BANTON, 273 U. S. 418.

A New York statute attempted to fix the resale price of theatre tickets, and declared the business of reselling them was affected with a public interest. This court said:

"The mere declaration by the legislature that a particular kind of property or business is affected with a public interest is not conclusive upon the question of the validity of the regulation. The matter is always one which is open to judicial inquiry."

UNITED STATES v. EMERY BIRD THAYER CO., 237 U. S. 28.

It was held that the government could not levy a franchise or excise tax, upon the Emery Bird Thayer Company as "a corporation doing business in the United States" where its sole function was the receipt of rents and distribution thereof to its stockholders, the corporation owning only one piece of business property in the City of St. Louis.

ZONNE v. MINNEAPPOLIS SYNDICATE, 220 U. S. 187.

An attempt was made to collect the Federal Corporation excise tax from a corporation, the sole purpose of which was to hold title to one tract of land and distribute the rents therefrom to its stockholders. The court said:

"As we have construed the corporation tax law (*Flint v. Stone Tracy Co.*, 220 U. S. 170), it provides for an excise upon the carrying on or doing of business in the corporate capacity. We have held in the preceding cases that corporations organized for profit under the laws of the State, authorized to manage and rent real estate, and being so engaged, are doing business within the meaning of the law, and are therefore liable to the tax imposed.

"The corporation involved in the present case, as originally organized and owning and renting an office building, was doing business within the meaning of the statute as we have construed it. Upon the record now presented we are of opinion that the Minneapolis Syndicate, after the demise of the property and reorganization of the corporation, was not engaged in doing business within the meaning of the act. It had wholly parted with control and management of the property; its sole authority was to hold the title subject to the lease for 130 years, to receive and distribute the rentals which might accrue under the terms of the lease, or the proceeds of any sale of the land, if it should be sold. The corporation had practically gone out of business in connection with the property, and had disqualified itself by the terms of reorganization from any activity in respect to it. We are of opinion that the corporation was not doing business in such wise as to make it subject to the tax imposed by the act."

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CHARLES ELMO

IN THE

Supreme Court of the United States

NO. 10

OCTOBER TERM, 1936

JOSEPH H. BARWISE AND GEORGE THOMPSON, JR.
As Trustees of the Estate of Mrs. M. M.
(W. I.) Cook, Deceased.

Appellants

VS.

GEORGE H. SHEPPARD,
Comptroller of the State of Texas, Et Al

Appellees

APPEAL FROM THE COURT OF CIVIL APPEALS, THIRD SUPREME JUDICIAL DISTRICT OF TEXAS

APPELLEES' SUBSTITUTE BRIEF

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(Reported 89 S. W. (2d) 1021 and 1026)

APPELLEES' SUBSTITUTE BRIEF

PRELIMINARY STATEMENT

At the last term of the Court, we filed a brief, hurriedly prepared in anticipation of an early setting, and without the benefit of appellants' brief, not then filed.

We have now been furnished with a copy of the latter; and we wish to substitute this for our former brief. We take it that it will be unnecessary for the Court to now consider the superseded brief.

We accept as substantially correct appellants' statement of the case, and the statutes and constitutional provisions, as set out in Appendix "A", "B", "C" and "D", pps. 32-56 of their brief.

The statement of the history of the suit, the pleadings, the substance of the material facts and the steps in the course of the appeal have all been fairly and adequately presented. We have no complaint on that score, although differing with counsel on the meaning and proper interpretation of certain stipulations upon which the case was tried. They refer to the relation of appellants to the business sought to be taxed and their real interest therein, and to the effect of the phrase "free of cost", as used in the contracts. The effect of these stipulations is briefly, but clearly, stated in the opinions of the Court below.

On page 12 of appellants' brief, we find a quotation in italics from the agreed Statement of Facts. Considered alone, it might be thought to sustain one of the points strongly relied upon; namely, that the statute, as applied, declared appellants to be producers, contrary to the fact and in violation of the stipulations of the case. We refer the Court to the opinions of the Court of Civil Appeals, wherein, in substance, it is held that the paragraph must be construed and considered along with the terms of the leases and all other admitted facts. So considered, it was properly held to

mean no more than that appellants were not *actively* operating or conducting the business; but that their interest therein and in the profits and success of the enterprise was real, direct and substantial. This and the other facts of record were considered as being sufficient to apply the law to appellants as producers within the meaning of the statute.

JURISDICTIONAL QUESTION

This case involves the validity of a tax statute of the State of Texas, challenged upon several grounds as violative of the Constitution of the United States. The salient and relevant parts of the statute, with convenient references, will be set out hereafter. We now have the benefit of appellants' brief in this Court. Their contentions are practically the same as made in the state courts, limited, of course, to the much narrower ground remaining after adverse decisions in the state courts on questions determinable and actually decided under the local law. The inquiry has been further limited by the abandonment by appellants of many questions raised below, as indicated in their statement of the points upon which they intend to rely here. (R. 60-61).

The grounds for jurisdiction in this Court are stated by appellants in the document styled: "Statement as to Jurisdiction", and in the beginning of their brief. While we have not formally challenged the jurisdiction of the Supreme Court, and while perhaps that course is not now open to us, we take it that the Court will exercise its power to refuse a decision on the merits, if of the opinion that no substantial Federal question

has been raised. It goes without saying that neither waiver nor consent of the parties can confer jurisdiction if none exists. We hesitate to say that the Federal questions sought to be raised here are frivolous and that, therefore, the case should be dismissed; but our doubts persist and we should be wanting in frankness if we did not say so. Upon the assumption, however, that the case is properly here for decision on the merits, we shall attempt to answer every point upon which appellants rely for a reversal of the decisions of the state courts.

ISSUES INVOLVED

To clear the way for the discussion of the points now remaining, we think it of some importance to call the attention of the Court to the fact that a number of questions arising under the State constitution and laws were raised below; but they were all decided adversely to appellants. 89 S. W. Rep. (2d) 1021-1028. Since they were all determinable by the local law and were actually decided by the State courts, it would seem that they are no longer in the case. They are thought to be concluded by the decisions and the interpretations placed by the State courts upon their own constitution, which are generally held to be binding upon the Federal courts. Furthermore, all such questions have been removed from controversy by the election of appellants to now rely solely upon the due process clause of the Fourteenth Amendment to the Constitution of the United States, and upon Section Ten of Article One of the Constitution, prohibiting any state from passing any law impairing the obligations of contracts. The Fifth Amendment is not here

involved, since it is well settled that it is a limitation alone upon the Federal power. What was said in our former brief concerning that Amendment was historical and for possible analogies in the purposes of adoption. We meant to imply nothing more. Nor do we understand that appellants have ever made any claim that the Fifth Amendment had been infringed by the legislation in question.

We think it will be conducive to the Court's convenience to make our replies to appellants' contentions under two headings: Due Process and Contract Obligations. Before proceeding to the discussion, it will make for convenience also to here set out the relevant provisions of the statute:

Approved May 22, 1933, it is an Act of the Legislature of Texas, known as House Bill 154, Chapter 162, Acts 43rd Legislature, Regular Session, page 409; effective August 29, 1933. It is a general revenue act, laying taxes not only on the business of producing oil, but on other unrelated occupations; the latter, of course, being irrelevant to this inquiry. We now quote the relevant parts: "There is hereby levied an occupation tax on oil produced within this State of two (2) cents per barrel of forty-two (42) standard gallons . . .". *Section* 2 (I)

"The tax hereby levied shall be a liability of the producer of oil and it shall be the duty of such producer to keep accurate records of all oil produced, making monthly reports under oath as hereinafter provided" *Section* 2 (2). "The purchaser of oil shall pay the tax on all oil purchased and deduct tax so paid from the payment due producer or other interest

holder, making such payments so deducted to the Comptroller of Public Accounts by legal tender or cashier's check payable to the State Treasury. Provided, that if oil produced is not sold during the month in which produced, then said producer shall pay the tax at the same rate and in the manner as if said oil were sold" *Section* 2 (3). "The tax herein levied shall be borne ratably by all interested parties, including royalty interests; and producers and/or purchasers of oil are hereby authorized to withhold from any payments due interested parties, the proportionate tax due." *Section* 2 (6).

It is not deemed necessary to set out any of the provisions of the Amendatory Act of the First Called Session, Chapter 12, as its effect is substantially stated in Appellants' Brief, p. 10.

A statute passed at the same session of the Legislature, being Chapter 214, and being found at page 637, Acts 43rd Legislature, Regular Session, provides the remedy for complaining taxpayers, through judicial processes. This Act, in substance, provides that any person wishing to contest the validity of the tax, or upon any other ground, may pay the same under protest. The administrative officers of the State are thereupon required to place the particular taxes involved in a special account, to abide the result of the litigation; and they are further required to put such funds out at interest in State depositaries, to draw the same rate of interest as State funds. The Act further provides a convenient forum for suits, including class suits, and expressly confers the right of appeal. If the complainant is successful, the law provides for a refund of the taxes withheld, with earned interest.

DUE PROCESS

We now proceed to the discussion of appellants' contentions. As to the claim that they have been denied due process of law, as guaranteed by the Fourteenth Amendment, there is, we take it, no fairer way to state them than to quote their exact words in specifying the points upon which they intend to rely. (R. 60-61):

1. "It being an admitted fact that the appellants are not engaged in the business of producing oil, the Texas Gross Production Tax law of 1933, as Amended, which arbitrarily provides that they are engaged in such business, to lay an otherwise prohibited tax upon them, contravenes the due process clause of the Fourteenth Amendment to the Federal Constitution."

2. "Appellants antecedent lease having obligated the lessees to deliver appellants' royalty oil to their credit in the pipe line free of cost, the tax law in question which authorizes and requires the deduction of two per cent of the proceeds of appellants' oil and the addition of a like amount to the proceeds of their lessee's oil, makes the appellants' royalty interest less valuable, and the method of enforcing the lease entirely different than when it was made, violates the due process clause of the Fourteenth Amendment to, and the obligation of contract clause of the Federal Constitution."

It may serve a useful purpose to cite some of the decisions of this Court, and to quote from other high

sources, upon what is due process, within the meaning of the Constitution.

Mr. Webster, in his justly celebrated argument in the Dartmouth College case, defined it thus: "As applied to judicial proceedings, due process of law means a law which hears before it condemns; which proceeds upon inquiry, and renders judgment only after trial".

Perhaps the most widely accepted definition is that of Judge Cooley: "Due process of law in each particular case means such an exertion of the powers of government as the settled maxims of law permit and sanction, and under such safeguards for the protection of individual rights as those maxims prescribe for the class of cases to which the one in question belongs".

Another definition, by this Court: "Due process of law, within the meaning of the Fourteenth Amendment, is secured if the laws operate upon all alike, and do not subject the individual to an arbitrary exercise of the powers of government". Leeper vs. Texas, 139 U. S. 468.

Still another: "Due process of law is so secured by laws operating upon all alike and not subjecting the individual to the arbitrary fiat of the power of government, unrestrained by the established principles of private right and distributive justice". Caldwell vs. Texas, 137 U. S., 697.

In our former brief, 11-14, we cited and quoted from several decisions by this Court, especially applicable to the taxing powers of the states, and to the limits of the restraints thereon found in the Fourteenth

Amendment. They are: McMillan vs. Anderson, 95 U. S. 37; Wade vs. Travis County, 174 U. S., 499; St. Louis vs. The Ferry Co., 11 Wall., 423; Kirtland vs. Hotchkiss, 100 U. S. 491; Memphis Gas Light Co. vs. Taxing District of Shelby County, 109 U. S., 398; State Tax on Foreign held bonds, 15 Wall., 319. We ask the Court to give them due consideration; and we cannot refrain from repeating the admirable condensation of the rule, as stated in State Tax on Foreign-held Bonds, supra: "Unless restrained by the provisions of the federal constitution the power of the state as to the mode, form and extent of taxation is unlimited where the objects to which it apprises are within her jurisdiction."

It was said in the case of Del Castillo vs. McConnico, 168 U. S. 674, that the federal courts derive no general jurisdiction from the 14th Amendment to the Federal Constitution to prevent or to relieve from oppression under states laws or to correct errors or mistakes of detail in state administration. Errors in the administration of a tax statute, not jurisdictional in character, will not justify the Federal Supreme Court in holding that the state has deprived or is about to deprive the complaining party of his property without due process of law. Lent vs. Tillson, 140 U. S. 316.

The 14th Amendment of the Federal Constitution, in declaring that no state shall deprive any person of property without due process of law, does not limit the taxing power of the states whatever the methods devised for the purpose of taxation, unless such methods by their necessary operation are inconsistent with the fundamental principles embraced by the re-

quirements of due process of law. Southwestern Oil Co. vs. Texas, 217 U. S. 114.

In French vs. Barber Asphalt Paving Co., 181 U. S. 324, the court said:

> "It was not the intention of the 14th Amendment to subvert the systems of the states pertaining to general and special taxation; that amendment legitimately operates to extend to the citizens and residents of the states, the same protection against arbitrary state legislation, affecting life, liberty, and property, as is afforded by the Fifth Amendment against similar legislation by Congress, and the Federal Courts ought not to interfere when what is complained of is the enforcement of the settled laws of the State, applicable to all persons in like circumstances and conditions, but only when there is some abuse of law, amounting to confiscation of property or deprivation of personal rights."

State cases upon which we rely are the following:

In the case of Flynn, Welch & Yates v. State Tax Commission, 28 Pac. (2d) 889, the Supreme Court of the State of New Mexico said in part:

> "Our minds do not reject the idea that the lessee and the royalty owner are considered as participating in a joint enterprise or both engaged in the business of producing or severing oil and that the tax is therefore essentially occupational. Such a view, however, is not indispensable to sustaining the tax. For it may be considered occupational as to the lessees and another kind of tax as to the royalty owner. Unless found as to one or the other to be a tax upon tangible property it need not be levied ad valorem and is excise."

The foregoing declaration of the Supreme Court of New Mexico was made at a time when the Supreme Court of that state had before it an attack upon the constitutionality of a statute of the State of New Mexico which is almost verbatim the same as the statute of the State of Texas which is now under attack by appellants.

Speaking further, and at the same time the Supreme Court of New Mexico said:

> "One cannot read the tax decision of the courts of last resort, state and federal, and fail to note an increasing resort for revenue to the occasion when the owner realizes upon the natural resources embraced within his land holding and by so doing depletes the taxable resources of the State."

We know of no state in the union whose wealth consists of rich natural resources that there is not some nature of tax upon the business of taking the minerals from the soil. The theory adopted uniformly by the states is that when once the vast stores of natural resources have been exhausted the otherwise taxable wealth of the state is gone; therefore, those who profit by the mining or production of minerals should contribute to the support of the government during the time when the minerals are being severed from the soil. Upon this theory appellants should be taxed for the reason that they will share in the profits of the exploitation of the minerals upon their land holdings in proportion to what they have invested as will the actual producer of such oil or other minerals. We think it may well be said in this case, as was said in the New

Mexico case, that appellants were jointly engaged with the lessees operating upon appellants' land.

In State vs. State Board of Equalization, 17 Pac. (2d) 68, the Supreme Court of Montana said, in effect:

> "Your operations deplete the natural resources of the State and to the extent that you remove from the earth the natural wealth with which nature has provided it and to that extent impoverish it, you are required to pay a license tax for the use and benefit of the state for the privilege of extracting such natural wealth. The tax provided is not, therefore, on metals, minerals or mined products, but rather upon the business of producing metals or precious stones based upon annual production."

An all-comprehensive definition of due process, decisive of all cases, is difficult to find; and this Court more than once has said that it is unnecessary and, perhaps, inadvisable to make the attempt. With no little confidence, however, we submit that the above cited definitions are sufficiently enlightening to decide this controversy. With their aid, let us proceed to examine appellants' claims.

The first point to be considered, we think, is the contention that the statute in question denies due process because of supposed arbitrary features therein, as applied to appellants. In reply, we assert that it would be difficult to find a law so solicitous for the rights of those subjected to its burdens. In respect to the remedy, it is almost meticulous in its processes and safeguards. A judicial hearing, adequate, comprehensive,

complete, is assured by its express terms; as indicated by the summary of the remedial statute, passed at the same session, as stated above. It would almost seem that the Legislature had due process of law directly and immediately in mind in passing these statutes. Certainly there is nothing lacking to make it what Webster conceived was due process of law: "A law which hears before it condemns; which proceeds upon inquiry, and renders judgment only after trial." We apprehend, however, that appellants will say that all this is beside the point; because these considerations go only to the matter of remedy, whereas their complaints are levelled at the substantive provisions of the law. We have no disposition to evade the issue. We shall meet the challenge upon that ground.

Before entering upon a detailed discussion, however, we again invoke the rule stated in Caldwell vs. Texas, supra: "Due process of law is so secured by laws operating upon all alike and not subjecting the individual to the arbitrary fiat of the government, unrestained by the established principles of private right and distributive justice". The language seems singularly applicable to the situation here. The tax statute, as revealed by even the most casual reading, operates upon all alike, within the just and reasonable classification of all owners of interests as producers, taxing each according to his actual interest. None of the incidences bears unreasonably upon any person or any class within its purview. None is subjected to the arbitrary fiat of the government, but the objects of the law bear a reasonable relation to the position of every owner of the business or the production taxed. In making the respective owners pay their proportion of

the tax, ratably, there is not only no denial of established principles of private right and distributive justice, but a clear recognition and enforcement of them.

We are not unmindful of the danger of employing generalizations, no matter how high the sources from which they come, as precedents to support contentions in another case. We recall the observation of Chief Justice Marshall, in Cohens vs. Virginia: "It is a maxim not to be disregarded that general expressions, in every opinion, are to be taken in connection with the case in which these expressions are used. If they go beyond the case, they may be respected, but ought not to control the judgment in a subsequent suit when the very point is presented for decision." If we have quoted or shall quote general statements not called for by the facts or issues of the case, it has not been by design. In each instance, we have thought the case sufficiently analogous and the quotation sufficiently appropriate to be of some value in the present inquiry. The learning and discrimination of your Honors can be relied upon to reject any specious references. These remarks are anticipatory; and while we are upon the subject, it may be remarked that the rule is not unilateral. It applies as well to general expressions cited by appellants. When convinced they are *dicta* or not in point, we shall freely state our differentiations. Appellants, of course, may do likewise.

Coming specifically to consider appellants' contentions under due process, we first take up the matter of the character of the tax. It is not deemed of any great importance to precisely describe the tax here imposed. We are of the opinion that it is best character-

ized as an occupation tax, having been levied upon the business of producing oil and measured according to the amount of oil produced, and ratably and proportionately against the owners of same. Although clearly occupational in character, it properly falls within the general classification of an excise, considered as either occupation, privilege or license tax. As stated by this Court in Hylton vs. The United States, 3 Wall. 171, the word "excise" has no precise meaning.

Having the general character of an excise, it was not necessary for the Legislature to classify or designate royalty owners as producers of oil, in order to validly tax them. It was sufficient, to differentiate the tax from a property tax, that the several owners of the oil, when severed from the soil and brought to the surface should be taxed in proportion to their interests in the production. The tax might well be regarded as one kind as to the active producer and another as to the royalty owner. It is clear that the Legislature did not intend to impose a property tax; least of all a tax upon the realty. The State courts so determined, when provisions of the Texas Constitution were invoked. Thus many of appellants' contentions are met.

Further pursuing the inquiry, in determining the character of the tax the true test is, not the name by which it is known, but the incidences of the tax. This rule has been frequently applied by this Court, and was recognized by the State court. The Legislature, however, called the tax an "occupation tax". While concededly not controlling, the legislative understanding is of importance. As was said by this Court, in Flint vs. Stone Tracy Company, 220 U. S. 145: "While

the mere declaration contained in a statute that it shall be regarded as a tax of a particular character does not make it such, the declaration of the law making power is entitled to much weight." In any event, if the tax is sustainable as being a proper exercise of the taxing power of the State, the fact, if it be a fact, that the Legislature gave it a mistaken or inappropriate name is wholly immaterial. Tested alone by its incidences, as appellants insist it must be, it reasonably appears to be a tax upon the business of producing oil. The many provisions relating to the imposition of the tax, the determination of the amount of oil produced and handled, the amount of the tax in every given case, the duties of the active producer in the matter of keeping records and making reports and the deductions and payments by purchasers, all bear directly and immediately upon the business. In levying the tax against the various interest holders in the oil produced, including the active producers and the royalty owners, the State court held that the legislature could validly declare the owners of royalty interests in the oil produced to be engaged in the occupation and business of producing oil. The State Constitution expressly authorizes the Legislature to levy occupation taxes. Therefore, it would seem that the question has been conclusively settled against appellants' contention, under the local law, as interpreted by the courts of the State. The power of the states to levy occupation taxes is not prohibited by the Fourteenth Amendment nor any other provision of the Federal Constitution of which we are aware. If not, it is difficult to see how any constitutional right of appellants has been infringed by the exercise of that power in respect to a business as to

which it is at least debatable whether every person having an interest therein, by way of royalties, or otherwise, is in fact engaged in the business.

Since it is insisted that the tax cannot be sustained, as to appellants, upon the theory that they are producers; because they in fact are not such, as has been expressly stipulated, and that the Legislature could not make them producers contrary to the fact, we feel impelled to examine the point a little more closely. We do not wish to evade in the slightest the force of our agreement, as disclosed by the Record. We stand by it fully, but it was made with reference to and in the light of other agreed facts, including the implied covenants of the leases. When all the facts and considerations and the circumstances relating to the production of oil are fully weighed, the stipulation means no more than that appellants are not producers, as that term is commonly understood. They do not actually produce the oil, but their interest in the business, as royalty owners, is such that the Legislature could reasonably adopt it as one of the bases of the classification. The leases are set out in the Transcript (R. 19-25). They are in the usual form of oil leases. The effect of these lease contracts was to make lessor and lessee partners in a joint enterprise, with different interests, it is true, but each having a direct interest in the success of the business. They are as truly partners as if named in the leases as such; not as general partners, but as to the particular undertaking. And the lessor is not even a silent partner, the leases appearing of record. For all practical purposes, he is, to the extent of his interest, engaged in the business of producing oil; and the Leg-

islature, in taxing such business, properly took his interest into account and taxed it ratably. That the active duties of production were imposed upon the lessee is not of controlling importance. As was aptly said by the Court of Civil Appeals (R.53):

> "We are also clear in the view that for the purpose of levying the gross production tax on the occupation or business of producing oil, the Legislature may validly declare the owners of royalty or other interests in the oil produced to be engaged in the occupation or business of producing oil. The ordinary form of oil lease has a dual character or purpose: 1. The conveyance of an estate in the land for development purposes; and 2. the future development and operation of the lease for oil in accordance with the terms (fol.66) express and implied, of the contract for the mutual benefit of the parties, their respective benefit being measured by the extent of their interests in the oil produced, or its value. The law is settled that the primary objective of the oil lease is the production of oil for the mutual profit of the parties. The consideration moving to the lessor is an interest in the oil or its value in money. Thus he has a direct interest in the success of the business. As the holder of the royalty interest the lessor or royalty owner is not only entitled to share in the gross production of the oil but may under the terms of the lease, express or implied, require proper, prudent and diligent management and development of the business, and has reserved and is entitled to both legal and equitable remedies necessary to enforce the obligations of the lease, and under some circumstances may forfeit the lease for non-development. Texas Co. vs. Davis, 113 Tex., 321; Robinson vs. Jacobs, 113 Tex., 231;

Thomason vs. Ham, 113 Tex., 238; Munsey vs. Marnet Oil and Gas Company, 113 Tex., 212."

We are not now concerned with technical partnerships, but only with finding a reasonable basis of support for the classification made by the Legislature, in treating royalty owners as part owners in the business of producing oil, along with all other owners. We have sought to regard substance rather than form, as, no doubt, did the Legislature. So viewed, we have no doubt that the true relation of holders of royalty interests to the business was ample warrant to class them, along with the active producer, as producers of oil; as was expressly done in Sections 2(2) and 2(6), considered together.

While convinced that the tax in question is an occupation tax, as declared by the Legislature and as decided by the State courts, we are not averse to discussing the legal effect if it should be regarded as a property tax. As we view it, the appellants would be little, if any, better off on that assumption. The right of the states to tax property within their limits has long since been settled beyond cavil. Indeed, it is a right inherent in the sovereignty. Texas has expressly recognized and authorized the exercise of this power in her constitution. Certain limitations on the power are also to be found in the Constitution, but the lower courts, in this case, have found adversely to appellants' contentions that these limitations have been violated. These holdings, predicated as they are upon the local law, are thought to be controlling on this point and binding upon this Court. If the question were still open, however, it must be limited to supposed infringe-

ments of the Fourteenth Amendment. Appellants, in bringing their case here, have so narrowed their claim. (R.61). The claims of impairment of contract obligations are upon different grounds, as we view them, and will be considered further on.

So we come to consider the restraints of the Fourteenth Amendment as they relate to the validity of this tax statute, considered as a property tax. We confess to great difficulty in finding even the narrowest ground for argument. There are no requirements in the Amendment, even by implication, for uniformity, equaltity or the amount of tax a state may impose upon property within her limits. It has long been settled law in Texas, as held by the Court of Civil Appeals, and the authorities cited in its opinions, that oil when raised to the surface and severed from the soil becomes personal property. Considered as a tax upon such property, wherein has any constitutional right of appellants been violated? The classification of royalty owners with other owners, for the purposes of the tax, does not, of itself, present any constitutional question under the Fourteenth Amendment. The claim of denial of the equal protection of the laws has been abandoned and need not be considered. The terms of the statute, from caption to emergency clause, reveal not a single element of inequality, discrimination, confiscation, injustice nor other supposed constitutional vice. It is surprisingly well drawn, and, seemingly, scrupulously fashioned to provide due process of law. If the Legislature failed in this regard, it must be because of inherent difficulties. There is nothing arbitrary in classing royalty owners as part owners of the oil pro-

duced where, as here, their very contracts make them indisputably such; and the limitations that they are to be taxed ratably and according to their interests only would seem to meet every constitutional requirement, even if it should be assumed that the Legislature has given the tax an inappropriate name. The courts of the State are expressly declared open to any citizen wishing to test the validity of the law, with right of appeal as in other cases; and their property and rights fully protected, pending the final disposition of suit. Even class suits, with their manifest advantages to all who are not active litigants, are authorized. The conclusion is ineluctable that, substantively and remedially, the statute does not offend against the Fourteenth Amendment.

A further contention of appellants is that the tax is void, as applied to th[illegible]ecause it lessens their income from the oil production covered by their contracts; and further, that the statute, as applied takes a part of their property and, in effect, gives it to their lessees. These propositions are more appropriately referable to their claim of impairment of contract obligations, and we shall treat them more fully under that head. However, since they are included in their invocation of the due process clause, we shall pause long enough to briefly give our answer here. As to depletion of income, by the imposition of the tax, we must be excused for saying that that is one of the unpleasant, indeed inevitable, things about all taxes. They will cut into our income, but that presents no legal question. The second point is even more untenable, if possible. The fact that under prior laws

the lessee, that is the active producer, was required to pay all the tax, although he might own less than the whole of the production (usually 7/8) and that under the present statute he pays only proportionately, according to his actual interest, falls far short of demonstrating that the appellants' property has been taken and conferred upon another. The share of the tax appellants now pay, as royalty owners, belongs to the State and to the State alone. The fact that the active producer has benefitted by the change in legislative policy is entirely beside the question. The new legislation seems to be nothing more than a belated recognition of the injustice of the old. These considerations, briefly stated, should be sufficient to show that due process has not been even remotely denied, in the particulars claimed. As stated they will be discussed more fully under the claim of contract impairments.

CONTRACT OBLIGATIONS

We now pass to the claims of impairment of contract obligation. Appellants assert that because of antecedent contracts, to which neither the State nor appellees were parties, the hands of the State were stayed and its taxing power subordinated to their private contracts; merely because their income from the particular enterprise was reduced by the necessary operation of the statute under consideration, and the further claim that the other parties to the contracts were benefitted by the change in legislative policy. If this were true, it would not suffice to destroy the statute; but the very novelty of the claim attracts. No ap-

plicable authority is cited, and the extent of the implications serves to refute the proposition. It really goes to the point that private contracts may have the effect of restraining the right of the States to exercise its taxing power to tax the business of using and enjoying its richest natural resource, through otherwise valid and lawful enactments. The contract clause of the Constitution contains no such limitation. To hold that it does would be to virtually destroy the taxing power over many subjects of taxation, to which the states are constantly and progressively resorting for revenue and as compensation for draining their natural resources. This Court, in Murray vs. Charleston, 96 U.S., 444; 24 L. Ed. 760 (a case cited by appellants) has said: "We do not question the existence of a State power to levy taxes as claimed, nor the subordination of contracts to it, so far as it is unrestrained by constitutional limitation." The mere assertion that contract obligations have been violated is not enough. It must be made to appear that the law under attack, in its necessary or enforced operation, alters the terms of a contract by imposing new conditions or depriving the parties of the means which the law in existence at the time of the contract afforded for its enforcement.

We apprehend that appellants, nevertheless, will insist that, notwithstanding the subordination of contracts to the taxing power generally, their case presents an exception and a limitation on that power, because the statute impairs the obligations of their contracts, in violation of the Constitution of the United States. The precise point, as we understand it, is that the law in question authorized and requires the deduction of a

part of the proceeds of their oil and gives the lessee the benefit of such deductions; in violation of a term of the contracts, whereby it was expressly stipulated that the lessee should bear the burden of the entire tax, by virtue alone of a provision therein that the lessee should delivet appellants' share of the oil or its proceeds, "free of cost". This contention requires a consideration of the terms and effect of the contracts, and whether any obligation thereof has been impaired by the statute, within the meaning of the Constitution. To this there are several answers.

We insist that the obligation of the contracts claimed to have been changed by the terms and effect of the statute has neither been impaired nor affected by the law. First, we deny that the contracts relieved appellants of the duty of paying their share of any tax the State might thereafter impose. Such an effect is claimed solely because of the inclusion of the phrase "free of cost". In the contracts, no specific reference is made to taxes. Indeed, they were not even in contemplation of the parties; therefore, no obligation in reference thereto was imposed. The tax statute in effect at the time of the contracts levied no tax upon the interest of royalty owners. It was wholly upon the active, operating producer; and he was required to pay the entire tax, notwithstanding he might own less than the whole of the production. This policy was changed by the Legislature in the enactment of the statute here assailed. It is difficult to perceive that the tax burden, now for the first time laid upon the royalty owner, according to his proportionate interest, was within the contemplation of the parties or intended to be included by the use of the phrase aforesaid.

To so infer is to impute to them a quality of prescience that would be truly remarkable; especially since there is nothing to show that a future legislature or legislators had in mind any change in legislative policy. If future taxes to be levied upon appellants were not in the minds of the parties, how can it be said that an obligation with relation thereto was created? If not, there was no obligation with respect thereto to be impaired. It is not claimed that any other term of the contracts had the effect of placing upon the lessee the duty of paying future taxes laid upon appellants.

We think the phrase "free of cost", as used in the contracts, must be taken to mean the usual costs of production; such as providing machinery, labor, drilling operations, bringing the oil to the surface, handling and saving, delivery to pipelines and other expense incidental to the actual production and marketing of oil. The payment of taxes is not ordinarily an expense of production; especially, we think, taxes imposed upon some one other than the producer, as commonly understood. Such an item would not be brought within the contract, unless specified; and the general phrase relied upon is, in our opinion, not sufficient for that purpose. Especially is this true, when constitutional limitations are urged to destroy the effect of a tax statute; and where the burden is upon the party assailing it, to point out the very contract obligation which it is said has been impaired. In such a case no doubtful constructions will be admissible. Hence we say that no obligation with reference to the payment of appellants' taxes was embraced in the contracts and, therefore, no such obligation impaired.

As we have said before, and we still maintain, appellants might just as soundly contend that the lessee under the contracts, could be required to pay the ad valorem tax upon appellants' realty, consisting of the undiscovered and undetermined minerals, as one of the costs incidental to the production of oil, as to make the claim that any future tax which the State of Texas might see fit to levy upon appellants, as an excise, should be borne by the lessee. We also reiterate that the tax now required by the laws of the State of Texas to be paid by appellants is no more a cost incident to that production than is the ad valorem upon a farm an incident to the cost of production of agricultural products. It will certainly not be contended that a tenant farmer, having a contract with his landlord to deliver, free of cost, every fourth bale of cotton (a practice common to such relations) assumes the obligation to pay all or any part of the landlord's taxes, by virtue of the clause relating to costs. Where is the difference in principle? We would not consciously bolster our arguments with fanciful analogies, nor with arguments and illustrations drawn from extremes. We think those just suggested are well within the spirit of the point under discussion.

Next, we reply that even if the agreement of the lessee to deliver appellants' share of the oil produced from their lands, free of cost, included the obligation to pay taxes of the lessor, still there has been no impairment of that obligation by the statute in question. If a tax not imposed and not contemplated at the time of the contracts could be said to be within the purview of the contracts, this statute does not affect the ob-

ligation. As was said by the Court of Civil Appeals: (R.56): "Manifestly this taxing act does not change in any manner the lease contracts between the parties. The tax is not against the oil royalty. It is levied as a gross production tax on the business or occupation of producing oil". It may be added that the statute does not affect the contracts at all. They remain exactly as before. If the lessor had succeeded, by the terms of the contracts or by their general effect, in obligating the lessee to pay all taxes, present or future, including those of appellants, what is there in the statute to prevent the enforcement of the obligation? It approaches subtlety to say that a mere change in legislative policy, whereby each owner of interests in the business of producing oil is made to bear his just share of the tax, relieves a party to the contract of his obligation to discharge a burden which he had voluntarily assumed. This belated recognition by the Legislature of the injustice of requiring a part owner of the business to pay all the tax affords no ground for saying that it was intended or has the effect of relieving such party of his contract obligation. The new policy is entirely independent of contracts, and all the provisions of the statute operate to enforce that policy, as between the state and each owner of interests in the business. By this we mean that there is nothing in the record to suggest that the Legislature had any purpose to disturb existing contracts; yet we do not concede that it did not have the power to do so, if it had deemed it necessary in order to bring its tax system into a just relation with its citizens, and to insure distributive justice.

It is even more unconvincing to assert, as appellants

persist in doing, that the effect and necessary operation of the statute is to take from them and give to the lessee. The statute is not capable of any such construction. Again the Court of Civil Appeals has adequately, if briefly, answered this contention. We quote, (R. 56): "The tax belongs to the State, and the mere fact that the producer is primarily liable for the payment of the tax, or the fact that the purchaser is required to collect the tax for the State at the source or origin does not give them any interest in the tax as against the royalty interests. They may have benefitted by the change of legislative policy of imposing the tax ratably against the respective interest holders in the oil produced; but such legislative tax policy did not impair any obligation of the lease contracts."

Elaborating somewhat on this clear statement, there has been no appropriation of appellants' property to the use or benefit of either lessee or purchaser; nor is that result possible under the act in question. All the tax for which they are liable goes to the State; and even its title is not complete until the termination of any suit they may elect to bring to test the validity of the law and the tax. The disputed tax remains in a special fund or account, deposited at interest for their benefit, to be refunded if their suit should be successful; otherwise to be covered into the State Treasury finally. Despite the attempt, apparently, to inject an element of misappropriation or confiscation into the case, the utter absence of any such vice is plain. The most that can be justly claimed by appellants is that they are now compelled to pay a part of the tax on the business, and that only because they are part own-

ers; whereas under the former law they would have had to pay no tax. What's wrong about that? Wherein does that deprive appellants of any right guaranteed by the Constitution of the United States? Surely it will not be contended that the parties could, as against the State, contract for immunity from taxation, present or future, or prevent the State from adjusting its tax system to what is later conceived to be in accordance with principles of private right and justice. Conceding that it was competent for them to contract that the lessee should bear the burden of appellants' taxes, as well as his own, and that they did so: the contracts, nevertheless, did not operate to restrain the State from levying a tax upon each owner, proportionately to his interest, and to collect it at the source. The matter of the enforcement of the contracts, as between the parties, is no concern of the State; their obligations, unimpaired by the act, remain as before. It becomes a mere matter of the proper interpretation of the contracts, if appellants should choose to demand a refund from producer or purchaser, as the case may be. In that controversy the State is not interested, nor can the enforcement of its tax laws be prevented, by any unfounded claim of contract impairment.

An additional word on alleged contract impairments. Quite aside from the consideration that the obligation, which appellants assert has been impaired, has no existence in fact, and forms no part of the contract, as we have attempted to show above, there is the further answer that the statute does not purport to and does not affect or impinge upon the contract as made by the parties. Effect upon any existing or future con-

tracts was not a legislative object, nor is there any evidence, intrinsic or otherwise, showing such a purpose. The contract, unaffected and unchanged, is not interferred with by the law; nor has there been any deprivation of remedy for its enforcement. The State courts properly reached these conclusions more fully stated above; there would be no excuse for elaboration.

In this relation, there is obviously no merit in the claim that because appellants, under a former law, paid no production tax on oil production, or on the business (a burden borne entirely by the lessee), they cannot now be made to bear their equitable share of the tax, under a new statute. The relation of appellants, by virtue of the leases, to the business in question is so real, so substantial that it affords a reasonable and just basis for the change in legislative policy. The prior immunity of appellants from any tax burden, either under existing statutes or under their contracts, is of no legal significance whatever. Neither is the voluntary assumption and payment by the lessee, as emphasized by counsel, under antecedent laws, at all important. Nor, as held by the Court of Civil Appeals, does the fact that the lessee is now required to pay one-eighth less of the tax than formerly, thereby increasing indirectly his net income, have any constitutional bearing, either under the due process clause or of that forbidding the impairment of contract obligations. That effect is only incidental, and is not an uncommon result of valid changes in taxing laws and systems. It is not, as often asserted by counsel: "taking one man's property and giving to another". It is not a taking at all; it is merely the adjustment of the State's

policy to obvious justice. It was never right to require the owner of only seven-eighth of a business to pay the entire tax for the privilege of pursuing it, or upon the production of it; at least it would appear that the Texas Legislature so concluded. Was there any vested right in the favored party to the continuance of that policy? Was the existence of *private* contracts securing such a right (if, in fact, they ever did), a constitutional obstacle to a change of public policy? We think the questions are answered by the mere statement of them.

Pages 20 to 27 of appellants' brief contain references to numerous cases, cited generally as illustrative of the limitations upon legislatures, the inconclusiveness of decisions of state courts and the right of independent inquiry by the Federal courts when Federal questions are involved. In deference to the zeal and ability with which Counsel has presented his cause, we concede a certain plausibility and persuasiveness in some of the general expressions employed and to his analysis. We insist, however, that a careful study of these cases will disclose that none is in point. Some we shall specifically differentiate; a generalization will suffice for the others.

We have not questioned and we shall not question the settled rules in this Court that state legislatures and Congress have no power, by mere designation, to declare a tax of one quality or character to have that of another; where the effect would be to deprive of constitutional rights. Nor that the effect of a law on rights secured by the Federal Constitution cannot be foreclosed by the decision of the state courts. Nor that

this Court decides for itself the nature and effect of a tax, regardless of the definition of it by the state court. Nor that the Legislature is without power to ignore substantial facts and convert, for taxing or regulatory purposes, a private carrier into a common carrier; a private business into a public utility, and the like, without regard to the essential facts. Nor to call a penalty or mere exaction a tax when plainly it is not. Nor that a congressional declaration that a certain Act regulated interstate commerce was effective, when it appeared that such was not its substantial effect. We simply say that this case presents no such unconstitutional aspects, and that it is not within any of the rules stated. The analogies, if any, are too remote.

The Texas cases cited, including Sheffield vs. Hogg (Tex. Sup.) 77 S. W. (2d), were considered by the Court of Civil Appeals and were regarded as presenting no obstacle to the validity and constitutionality of the statute. The Supreme Court of Texas, by denying a writ of error, in effect upheld this holding.

Appellants have cited and quoted from several decisions of this Court, in their brief and in their Statement as to Jurisdiction here. They are all thought to be distinguishable from the present case, and we shall point out the distinctions which occur to us in the principal cases cited. Other differentiations will doubtless occur to your Honors. If some of the general expressions quoted seem to give support to any of the contentions made by appellants, they do not apply here; and we must be pardoned for again recalling the maxim stated by Chief Justice Marshall in Cohens vs. Virginia, supra.

Presumably under their claim that they have been denied due process of law, and specifically that the tax here involved is a direct tax upon appellants' property right in the leased land, appellants cite Pollock vs. Farmers Loan and Trust Co., 157 U.S. 429. That case involved the validity of an act of Congress, imposing an income tax; and the tax was assailed as being a direct tax, violative of the apportionment and uniformity clauses of Article One of the Constitution. A further contention was that the tax was void because laid upon income from state and municipal bonds. The Court decided just two questions: 1. That the tax was a direct tax, as being a tax on rents or income of real property; and was void, as in violation of the Constitution. 2nd. As to the income from municipal bonds, the Act was void, on the ground that the United States have no power to tax either the instrumentalities or the property of a State. The chief controversy in that celebrated case seems to have raged about the distinction between "direct" and "indirect" taxes. Much was argued and much was written, but we have failed to discover anything of controlling significance here.

G. H. & S. A. Ry. Co. vs. Texas, 210 U.S. 217 merely decided that the Texas statute, levying the tax, was an attempt to regulate commerce among the states. The further incidental point, that the words "equal to" did not prevent the tax being an effort to reach the gross receipts, in part derived from interstate business, was also decided. No comment is necessary.

Flint vs. Stone Tracy Co., 220 U. S. 108, decided no more than that the "Corporation Tax", in the

Tariff Act of 1909, was not a direct tax but an excise. It is worthy of note, however, that in the opinion of the Court it was said that, while a mere declaration in a statute that a tax shall be regarded as of a particular character does not make it such, the declaration of the law making power is entitled to much weight. Other questions passed upon are manifestly irrelevant here.

Lake Superior Mines vs. Lord, 271 U. S. 577, decided that the Minnesota statute under attack was, in the absence of a decision by the State courts, a tax upon mineral estates in land; and that the statute did not offend the Fourteenth Amendment. If there be any persuasive features in the case, statutory differences and the fact that there had been no decision by the State courts, as to the character of the tax, lessen its force as a precedent. Much less is the actual decision, in the circumstances in which rendered and under the facts involved, a controlling influence in this controversy.

United States vs. Emery, 237 U.S. 28, involved the constitutionality of the Corporation Tax of 1909, as applied to a realty concern, whose only business was to keep up its corporate organization and to collect and distribute the rent received from a single lessee. It was held that the Company was not doing business within the meaning of the Act of Congress. Too remote, too remote!

Again presumably under due process, appellants cite Dawson vs. Kentucky Distilleries Co., 255 U.S., 288. The precise point intended, as we understand it, is

that a legislature cannot make a tax an occupation or license tax by merely calling it such—a proposition which we do not in the least controvert. The irrelevancy of the case appears from at least the following considerations:

The Kentucky statute there involved imposed a tax of fifty cents a gallon on whiskey withdrawn from bond or transferred in bond. Although termed an "annual license tax", it was not an occupation tax, but essentially a property tax, tested by the local law. Although levied on manufacturers of whiskey and those engaged in the business of owning and storing same in bonded warehouses, much of the whiskey affected was owned by citizens of other states, their ownership evidenced by negotiable warehouse receipts. The interpretation and validity of the statute had not, as here, been determined by any State court; hence the Federal courts felt free to decide the question upon the local law. It was held that the tax was essentially a property tax and, therefore, invalid under the Kentucky constitution. The facts showed that the act of various owners of bonded whiskey, in withdrawing it (the thing really taxed) had no relation to the business of buying and selling whiskey or otherwise using whiskey. The tax was imposed upon each lot of whiskey at the time of removal and the act of the owner in removing was actually the thing taxed. The emergency clause of the Act showed that the Legislature considered it was taxing the whiskey; hence, property. Is not the distinction manifest?

Upon impairment of contract obligations, appellants cite Murray vs. Charleston, 96 U.S. 432. These

grounds of differentiation from the case before the Court readily appear: The City of Charleston was a party to the contract, and it was its own contract the obligations of which were claimed to have been impaired. By its ordinances, the City sought to change the terms and obligations of its debt. The creditor was a non-resident owner and holder, he being a native of Germany. The Court, however, did not decide the effect, if any, of the creditor's being a non-resident holder of the credit involved.

Further, on the same points, appellants cite Cleveland P & A. R. R. Co., vs. Pennsylvania, 15 Wall., 82 U.S. 300. In that case the State of Pennsylvania sought to tax the interest on bonds of the Railroad Company, in the hands of non-resident holders. It was held that the bonds were property beyond the jurisdiction of the state; and that the alleged tax was but an exaction and forced contribution upon property held in other states. The difference is manifest.

Hartman vs. Greenhow, 12 Otto (102 U.S.) 672, was a case in which it appeared that the State of Virginia sought to avoid her own contract, whereby the State had contracted to receive coupons for all taxes to the State. The device of requiring the tax on her bonds issued under prior laws, to be deducted from the coupons originally attached to them, when tendered in payment of state taxes, was held to be an impairment of her contract with the bondholders and their assigns. The relation of the parties to the contracts alone suffices to distinguish. In any case, the decision is to be limited to the facts upon which it rested.

SUMMARY OF ARGUMENT

By way of recapitulation, and at the risk of repetition, we summarize our arguments as follows:

To appellants' claims that they have been denied due process of law, we reply:

That the statute under attack, together with the complementary remedial statute, passed at the same Session, affords due process to the fullest extent guaranteed by the Fourteenth Amendment. A speedy, adequate and comprehensive remedy is provided, in the specific provisions for a judicial hearing and review, extending to all legal questions which complaining taxpayers may see fit to raise. Pending the result of suits, the taxes paid under protest are held in a special account and placed at interest as are state funds, and at the same rate of interest. If the complainant is successful in his suit, his money with earned interest is returned to him. Considered remedially, the statutes would seem to meet every possible test of due process, within the meaning of the Fourteenth Amendment.

As to the substantive provisions, they deprive appellants of no constitutional right whatever. The taxes are laid for general revenue purposes and the burdens are distributed with fairness and equitably upon all subject thereto. The basic standard adopted is that of measuring the liability of every owner of a share in the gross production or business of producing oil, strictly according to his interest. Each is taxed ratably and in exact proportion to his ownership. There is no discrimination, no inequality, no confiscatory features, nothing arbitrary or capricious in the law, from caption to emergency clause. Wherein, then, have

appellants been deprived of any constitutional right?

The specific claim, so persistently advanced by counsel, that there has been a denial of due process, because the effect of the statute is to take from appellants a part of their property and to confer it upon the active producer in the business, is manifestly untenable. A casual reading of the statute will disclose no such purpose and no such effect. Not one cent of the taxes collected from royalty owners is for the use and benefit of the active producer or any other owner. It all goes to the state and to the state alone. We wish to be mindful of the amenities always, but the contention seems almost fanciful. It must rest, we think, solely upon the consideration that under former tax laws the active producer had been made to bear the entire burden of the tax, notwithstanding he might and usually did own less than the whole of the production; whereas under the new statutes he was made to pay the tax only according to his ownership; and the remainder, if any, is required to be borne by the other owners, according to interests. This, in effect, is to argue that a citizen without the purview of a taxing system at a given time, is, by some strange process of reasoning, protected by the Fourteenth Amendment from ever being brought within its burdens. In other words, that the Constitution gives him perpetual immunity from taxation, otherwise lawful and within state constitutional authority. The statement of the claim is its own refutation.

As to claims of impairment of contract obligations, we have several answers: First, we reply that the obligation said to have been impaired never had any existence. Neither the terms of the contract nor its im-

plications embraced the obligation of the lessee to pay the taxes here in dispute. The contention that they did rests wholly upon the clause in the contract that lessee should deliver to appellants their share of the oil produced "free of cost". Neither this phrase nor anything else in the contract indicates that the taxes of appellants, least of all taxes under laws not yet passed nor even contemplated by the Legislature, were thereby assumed by the lessee. The words must be taken in their usual and ordinary signification. So confined, they mean nothing more than the customary and usual costs incidental to the production of oil. They are not adequate to embrace a liability of the owners to the State for taxes. Such a charge has no relation to the production of oil, save as that activity or the business thereof affords the basis for the levy of the tax. It is not a cost incident to the production, as that term is commonly understood. Hence we say that there was no such obligation to be impaired.

Next, we say that, even if the payment of appellants' taxes could be said to be an obligation on the part of the lessee, by virtue of the terms of the contract, express or implied, the statute does not purport to impair or even affect that obligation. The contract remains as before, wholly unaffected and unimpaired. Such was the construction given by the Court of Civil Appeals, and so interpreted, all the constitutional rights of appellants were preserved and protected.

Finally, we conceive that appellants' contention goes to the indefensible point that the power of the state to tax is to be subordinated generally to private contracts, to which it is not a party; when the object

of the tax legislation is the raising of revenue from persons or property within her limits and under the authority of the State Constitution. Conceding, as we must, that the exercise of the taxing powers of the state is not beyond the restraints of the Federal Constitution, we contend, nevertheless, that when those powers are exercised in conformity with state constitutions and the taxes are levied upon property or persons within the state's jurisdiction and limits, the mere existence of antecedent private contracts does not, of itself, present any Federal question of contract impairments. Cases have been found and will continue to be found in which state taxing statutes must fall, because they impair the obligations of contracts; but all such will be seen to contain constitutional objections not here present. If such a convenient device, in private contracts, as the assumption by one party of the taxes of the other could operate, by force of the Federal Constitution, to exempt the latter from the tax laws of the state, we should expect to see the practice become very general. If by mutual agreement each party to a contract assumes and agrees to pay the taxes of the other, and the effect would be to deny the state the right to collect from either the taxes lawfully imposed upon them, because of resulting impairments of contract obligations, it is easy to see that the state would be seriously embarrassed in the raising of necessary revenue and in the devising of a tax system which should bear fairly and justly upon all alike. The Federal Constitution does not have and has never been given this meaning. We apprehend that the Court will not give it now. The power of the state to tax, within constitutional limits, extends to all persons and all prop-

erty within her borders; and is not to be circumvented by so easy a device as is here employed to accomplish that result.

Convinced that no constitutional right of appellants has been violated, under either the Fourteenth Amendment or the First Article of the Constitution, we pray that the judgment of the Court of Civil Appeals be in all things affirmed.

This argument is substituted for that made in our brief, heretofore filed, and we request the Court to consider it in that relation. We also ask the Court to give due consideration to the well considered opinions of the Court of Civil Appeals. (R. 45-57). We are sure they will be of aid in deciding some of the questions here.

Respectfully submitted,

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CHARLES ELMOR

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM A. D. 1936

NO. 10

JOSEPH H. BARWISE AND GEORGE THOMPSON, JR.
AS TRUSTEES OF THE ESTATE OF MRS. M. M. (W. I.) COOK, DECEASED.

APPELLANTS,

VS.

GEORGE H. SHEPPARD,
AS COMPTROLLER OF THE STATE OF TEXAS, ET AL.,

APPELLEES.

APPELLANTS' PETITION FOR REHEARING

WILLIAM R. WATKINS,
FORT WORTH, TEXAS,
ATTORNEY FOR APPELLANTS

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APPELLEES.

APPELLANTS' PETITION FOR REHEARING

Appellants pray a rehearing herein, and as grounds respectfully represent:

We do not question the power of the State to lay an

excise on the production of oil, or to apportion it on those who engage in the production of oil.

---

1. Defining excises, Mr. Justice Field in Pollock v. Farmers' Loan & Trust Co., 157 U. S. 429, 592, said:

> "Excises are a species of tax consisting generally of duties laid upon the manufacture, sale, or consumption of commodities within the country, or upon certain callings or occupations, often taking the form of exactions for licenses to pursue them. The taxes created by the law under consideration as applied to savings banks, insurance companies, whether of fire, life, or marine, to building or other associations, or to the conduct of any other kind of business, are excise taxes."

Taxes on the use of carriages, Hylton v. United States 3 Dall. 171, on sales at exchanges or boards of trade, Nicol v. Ames, 173 U. S. 509, on the transmission of property from the dead to the living, Knowlton v. Moore, 178 U. S. 41, on agreements to sell shares of stock, denominated "calls" by stock brokers, Treat v. White, 181 U. S. 264, on tobacco manufactured for consumption, Patton v. Brady, 184 U. S. 608, on manufactures of cheese, Cornell v. Coyne, 192 U. S. 418, on the sale of oleomargarine artificially colored, McCray v. United States, 195 U. S. 27, on sale of shares of corporations generally, Thomas v. United States, 192 U. S. 363, on the business of transfer companies, Binns v. United States, 194 U. S. 486, on the amounts insured, renewed, and continued by insurance companies, on the gross amounts of premiums received, on dividends undistributed sums, and income, Pacific Ins. Co. v. Soule, 7 Wall. 433, on the amount of state bank notes paid out by banks, Veazie Bank v. Fenno, 8 Wall 533, on devolutions of title to real estate, Scholey v. Rew, 23 Wall, 331, and on the gross receipts of companies engaged in refining sugar, in excess of a named sum,

But, appellants, as lessors, have no community of interest or joint relationship or joint ownership or common right in the undertaking engaged in by their lessee.[2] The language of the opinion defines their relation to be that of partners.[3] The lessee's purpose is entirely distinct and independent and appellants have no reciprocal or mutual relationship thereto, or share in the profits as such.[4]

Spreckles Sugar Refining Co. v. McClain, 192 U. S. 297, have all been upheld as excises.

2. See notes 5, 7, 10, 15, 16, 18, 19, 20, 24, 25, 27, 37, 38, 39.

3. "Those persons are partners, who contribute either property or money to carry on a joint business for their common benefit, and who own and share the profits thereof in certain proportions." Meehan v. Valentine, 145 U. S. 611, 623.

See notes 18, 19, 24, 25, 27, 37, 38, 39.

The opinion in this case states: "The lease shows that the parties to it are, in a very practical sense, committed to and engaged in a common venture for their mutual benefit. The lessors have put into the venture their right to explore for and to extract the oil under their lands, and the lessee has put into it various drilling and pumping appliances and much expense, labor and time. All that has been put in is devoted to the common purpose of producing oil in which the lessors and the lessee are to have stated interests. It is this production that is taxed against the lessors and the lessee according to their respective interests."

4. See notes 5, 7, 10, 11, 13, 14, 15, 16, 18, 19, 24, 25, 27, 38, 39.

FIRST. The oil and gas lease is in reality a grant

5. Texas Co. v. Daugherty, 107 Tex. 234, 176 S.W. 717, L. R. A. 1917-F, 989, Stephens County v. Mid-Kansas Oil & Gas Co. 254 S. W. 290, (Sup.) in which the Court said: "The opinion in that case (the Daugherty case) leaves no room for reasonable doubt as to the soundness of the conclusion that gas and oil in place are objects of distinct ownership and sale as a part of the land. * * * Ownership of the gas and oil in place meant having the exclusive right to possess, use and dispose of the gas and oil. The *grantors* were clearly divested of the right to either possess, use, or dispose of the gas and oil in place in the lands described in the instruments here involved as soon as the instruments were executed. At the same instant, the right to possess, use and dispose of such gas and oil in place passed to the *grantees* in said instruments and to their assigns. Complete divestiture of title to the gas and oil could hardly be more completely evinced than by the necessity for an express reservation of even enough gas for domestic use in the grantors' dwellings. Dominion over a thing could not well be completer than it is in those persons who may, at their will, assign it to any other, with or without consideration, for a time which may be forever." The leases thus construed are not different in substance than those in the record in this case, and the court observed that any instrument which showed a purpose to grant the right to take the oil would be similarly effective.

Brewster v. Lanyon Zinc Co., 140 Fed. 801, 807, in which Mr. Justice Van Devanter, while on the Circuit said: "Although the parties, with the sanction of a general practice, denominated the instrument a 'lease,' strictly speaking it was not such, but was more in the nature of a grant in præsenti of all the oil and gas in the lands described—these minerals being part of the realty—with the right to enter and search for them, and to mine and remove them when found."

which may continue forever, but which may also terminate upon cessation of use thereof for the production of oil and gas; it creates an estate in land "called a base, qualified or determinable fee," defined by Kent as "an interest which may continue forever, but the estate is liable to be determined, without the aid of a conveyance, by some act or event, circumscribing its continuance or extent.' "[6]

SECOND: All the interest which the lessor has is real property. The so-called royalties are in reality payable as rent[7] and constitue the consideration[8]

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6. Stephens County v. Mid-Kansas Oil & Gas Co., supra, Waggoner Estate v. Sigler Oil Corporation, 118 Tex. 517, 19 S. W. (2) 27, Sheffield v. Hogg, infra n 10.

7. Von Baumback v. Sargent Land Co., 242 U. S. 503, 522, where it was said that the sums payable to a lessor under a mining lease "were in facts rents or royalties to be paid upon entering into the premises and discovering, developing, and removing the mineral resources thereof, and as such" are income, under the corporation tax law, to be taken into account in determining the amount of tax payable by a corporation "engaged in business." The Court held the lessor corporation in this case subject to the excise, not because of the mere receipt of the rentals, but because it was actively engaged in business within the meaning of the law.

Guess v. Harmonson, 4 S. W. (2) 124, in which it is held that: "Royalty is another term for rent, but is limited to rents due for the right or privilege of taking minerals, oil or gas out of a designated tract of land."

Hill v. Roberts, 284 S. W. 246, 249, in which it is

for the grant. This is true whether the rent be considered as payable in the form of service,[9] that is, for delivering the lessor's royalty oil, or whether it

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said that: "The word 'royalty' as used in a gas lease, generally refers to 'a share of the product or profit reserved by the owner for permitting another to use the property.' "

Sheffield v. Hogg, 77 S. W. (2) 1021, infra n. 10.

For other similar definitions see Glassmire "Law of Oil and Gas Leases and Royalties" (1935) Sec. 11.

8. Freeport Sulphur Co. v. American Sulphur Royalty Co., 6 S. W. (2) 1039, 1043, in which it is said that: "It is apparent, however, that the royalty contracted for and the $1 per ton on 200,000 tons on first production was at least a *consideration* specifically provided for. * * * The royalty of 75 cents per ton on all sulphur produced and the additional $1 per ton on the first 200,000 tons mined were a part of the consideration for the sale of the property."

9. Mills-Willingham, Law of Oil & Gas, pp. 173-8: "At common law it was quite competent to make a rent service or rent charge the entire consideration for the transfer of an estate in fee. The character of the rent thus reserved does not appear to have been materially altered by the fact that it was purchase price. Nor does the law appear to have distinguished between rents proceeding from ordinary usufruct and those proceeding from a part of the corpus. Both were a profit or rent. Both were inseparably connected with the land so that a grant of all the rents and profits was a grant of the land itself."

Blackstone's Commentaries, Vol. II, p. 41, infra n. 11.

be considered that the royalty oil itself is the rent.[10]

10. In Sheffield v. Hogg, 77 S. W. (2) 1021, the Supreme Court of Texas had under consideration the question whether the royalty interest of a lessor was taxable as realty, in the county where situated, or as personalty in the county of the owner's residence. Some of the involved leases provided for payment of royalty in kind, others for the payment of a stipulated amount based on production. The Court said: "The question before us is: What was the interest of the lessors under the instruments through which they claim in each of the cases now before us? Despite differences in their phraseology and forms, we have concluded after careful consultation and deliberation, that the lessors interest, sought to be taxed in each instance, or that of his assign, was an interest in land, subject to taxation as such in the counties in which the respective tracts of land are situated." "*All the property interests of ascertainable value, secured to the lessors or their assigns * * * are subject to taxation as real estate in the county wherein the land lies.*"

This holding was not made without the gravest consideration, it is fortified by a historical background in Texas jurisprudence which proves indisputably that ALL THE LESSORS INTERESTS under the lease are REAL PROPERTY.

The Court quoted approvingly from the opinion in United States v. Noble, 237 U. S. 532, 533, in which the question was whether restrictions on alienation of allotted Indian land, applied to royalty reserved under a valid lease thereof in which this Court had said: " 'The rents and royalties were profit issuing out of the land. When they accrued, they became personal property; but rents and royalties to accrue were a part of the estate remaining in the lessor. * * * ' " Continuing, it said:

"The principle underlying the determination in U.

Signification of the lessor's interest as rent, refutes

S. v. Noble supra, that the mineral royalties there under discussion constituted interest in land, had been announced in that tribunal as far back as 1823, when in an opinion by Mr. Justice Washington, the Court said: "A right to land essentially implies a right to the profits accruing from it, since, without the latter, the former can be of no value. Thus, a devise of the profits of land, or even a grant of them, will pass a right to the land itself. Shep. Touch. 93, Co. Litt. 4 b. 'For what' says Lord Coke, on this page, 'is the land, but the profits thereof.' Green v. Biddle, 8 Wheat. 1, 76.

"On the subject of rents and profits from lands, Mr. Thompson says:

" 'Rent is said to be a certain yearly profit arising out of lands and tenements as compensation for the use thereof. * * *

" 'Thus, if the grantor conveys a fee simple title in the lands, reserving rent, he himself has a fee simple in the rent. * * * A rent reserved upon a conveyance of land with words of inheritance, is real property and passes to the heirs of the grantor. * * *'

"Mr. Tiffany is in full accord with Mr. Thompson. According to Mr. Tiffany: 'A rent reserved on the grant of a fee simple estate in land is real property.' * * *

"On the subject of taxation of interests under oil and gas leases, Mr. Summers significantly notes that:

" 'Where, under the ordinary lease, the lessor retains a certain share of the oil or gas as a royalty, the value of such interest may be added to the agricultural value of the land for the purpose of making the assessment.' "

See Carpenter v. Shaw, 280 U. S. 363, infra n. 16.

the idea that there is a community of interest.[11]

Not only is it the law of Texas that "ALL THE PROPERTY INTERESTS * * * SECURED TO THE LESSORS * * * ARE SUBJECT TO TAXATION AS REAL ESTATE IN THE COUNTY WHEREIN THE LAND LIES,"[12] but this construction of the statutory definition of real property[13]

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11. Blackstone's Commentaries, Vol. 2, p. 41:

"The word rent * * * signifies a compensation or return, it being in the nature of an acknowledgment given for the possession of some corporeal inheritance. It is defined to be a certain profit issuing yearly out of lands and tenements corporeal. * * * It may also consist in services or manual operations; as, to plough so many acres of ground, to attend the king or lord to the wars, and the like; which services in the eye of the law are profits. * * * It must issue out of the thing granted, and not be part of the land or thing itself; wherein it differs from an exception in the grant, which is always of part of the thing granted. * * * A rent cannot be reserved out of an advowson, a *common*,[a] an office, a franchise or the like."

a. (COMMON—The right of taking a profit in the land of another, in common either with the owner or with other persons—so called from the community of interest which arises.—Webster Dict., Bouvier's Law Dict.)

12. Sheffield v. Hogg, n. 10, supra.

13. Art. 7146, R. S. 1925: "Real property for the purpose of taxation, shall be construed to include the land itself, whether laid out in town lots or otherwise, and the buildings, structures and improvements, or other fixtures of whatsoever kind therein, *and all the rights and privileges belonging or in any wise appertaining thereto, and all mines, minerals, quarries and fossils in and under the same.*"

which was one of the considerations that lead the Court to hold in Sheffield v. Hogg, supra, that ALL of the lessor's rights are real estate[14] is grounded deep in our law.

It has long been settled by cases cited in that opinion or to which the cited cases refer, that the rights, franchises and privileges incident to the ownership of land are substantially a part of it,[15] and that such

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14. In Sheffield v. Hogg, supra, the Court said (p. 1030): "Reading the Constitution and statutes together; there is no escape from the conclusion that the interests herein involved are meant to be taxed as real estate. Classify them as you may, they are at least rights or privileges belonging or in some wise appertaining to real property, and the Legislature has provided that they be taxed as such."

15. In Texas Company v. Daugherty, supra, the Court, after quoting the statute (supra n. 13), said that: "The rights and privileges belonging to land contribute in a very substantial way to its value. They largely cause it to yield its income, and it is the theory of our statute, therefore, that their value shall be included in the valuation of the land for taxation in the hands of the owner. They do not escape taxation by this method; on the contrary they are subject to its burden through the inclusion of their value in the assessment of the land; and they are taxed against the owner of the land because the Legislature has deemed it proper for him to bear their charge in view of their essential contribution to its value." Citing State v. Austin & N. W. R. R. Co., 94 Tex. 530, 62 S. W. 1050, in which the Court, construing the same Article of the Statutes, said:

"It seems to us the plain purpose of the article last

rights are to be carefully distinguished from the pur-

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quoted (is) to require that in assessing real estate for taxation, whether held by a natural person or a corporation, there shall not only be included in the valuation the value of the land itself merely as land, together with the improvements thereon, but also all franchises and privileges appurtenant thereto, and all the advantages for a profitable prosecution of the business to which it is appropriated. As a rule, the value of improved real estate is proportionate to the net income which it will yield. * * * In valuing a railroad for taxation, the valuation should include every right and privilege which was exercised in producing its income, and * * * it was not intended to disassociate the soul from the body of the living concern, and value by itself the lifeless remains. If we are correct in this conclusion, then it follows that it was not the intention of the Legislature to tax the franchise of the railroad separate from its real estate. TO SO TAX IT WOULD LEAD TO DOUBLE TAXATION, WHICH IS NOT PERMITTED."

But the Court did not fail to discriminate between the franchises that are inherent in ownership of property, and those which exist independent thereof, and are separately subject to an excise. It said that among the personal property required to be listed for taxation are *franchises*, and the value thereof, and that such franchises are " 'special privileges conferred by the government on individuals, and which do not belong to the citizens of the country generally, of common right.' * * * Under this definition it seems to us that the ordinary franchises of a railroad corporation are the right to exist and to transact business as a corporation, and the right to condemn property to its uses."

suit of an occupation—the lawful subject of an excise—in which property may be employed.[16]

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16. In State v. G. H. & S. A. Ry. Co., 97 S. W. 71, 77, the Court said:

"The fact that the franchise is subject in this state to an ad valorem tax as property does not militate against the right to tax the persons or the corporations using that property as an occupation any more than would the taxing of the physical property of the railroads, as the tracks, right of ways, cars, etc., operate to prevent the imposition of occupation taxes for the use of them as instruments of transportation. * * * As well might it be held that an ad valorem tax upon a storehouse, fixtures, and goods would preclude an occupation tax upon the merchant for pursuing the business of selling the goods."

"Since a corporation can carry on no business except that for which it holds a franchise from the state, it follows that *any tax levied upon a corporation in this state for exercising the privilege of carrying on its business must be classed as an occupation tax under our constitution, and in all tests of the validity of such a tax, those provisions of the Constitution which apply to occupation taxes must be the standard.*" (Citing Article VIII, Sec. 1 of the Constitution, which is quoted on page 53 of our original brief).

In Producers' Oil v. Stephens, 99 S. W. 157, it was held with respect to the original gross production tax on producers of oil that:

"The tax is not upon the gross products of the oil wells, but upon the occupation of owning, controlling, or managing oil wells, producing oil; and the amount of the tax is measured by a percentage of the market value. * * * Although this law imposes an occupation tax upon the oil producers who pay an ad valorem tax upon the real estate producing oil, it does not constitute double taxation, not permitted by the law, as

An occupation is certainly not appurtenant to any

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it is within the authority of the Legislature to impose an ad valorem tax for the USE of this property in the PRODUCTION OF OIL."

Shortly thereafter in Texas Co. v. Stephens, 103 S. W. (Tex. Sup.) 481, 484, the Supreme Court had occasion to consider the holding in the Producers' Oil Company case. It said: In the case of Producers' Oil Co. v. Stephens, 99 S. W. 157, in which this Court recently refused a writ of error, the point was made that the tax levied by section 13 of the act under consideration upon producers of oil was a tax upon property; but the courts below held otherwise, and this Court in refusing the writ of error approved the holding. *The taxes in the act are levied because the persons specified are engaged in particular, defined businesses, and are laid upon the carrying on of those businesses. The amounts of the taxes to be paid by those engaged in the businesses are to be ascertained by various standards depending upon the character of such businesses, but in no instance is a tax laid upon all or any of the property owned by such persons.* Had the statute simply defined the business and imposed a tax of a fixed sum upon each, no one would have questioned that it was a tax upon the doing of the businesses; in other words, an occupation tax. The fact that the amount of the tax is to be determined in prescribed methods, from the value or extent, or magnitude of the businesses done, cannot convert it into an ad valorem tax upon the property of the persons conducting them."

Because the law laid the occupation tax equally upon all persons of the class selected to bear it, this Court affirmed the decision of the Texas court in a companion case (100 S. W. 489) Southwestern Oil Co. v. Texas, 217 U. S. 114.

Cf. Carpenter v. Shaw, 280 U. S. 363, in which this

particular property. If it clearly appears that a so-called excise falls on property, it violates our State Constitution, regardless of its characterization.[17]

Court held the Oklahoma 3% Gross Production Tax was a property tax on the lands of an Indian lessor which were exempt from taxation by Federal law. The Court said: "We think it plain that the tax * * * is, by its very terms, a tax upon the right reserved in them as lessors and owners of the fee. * * * The Oklahoma Courts * * * * have treated the royalty interest of the lessor as a right attached and incident to his ownership or reversionary interest in the land. * * * But even if this did not appear to be the case, an interest commonly so associated with the use and enjoyment of the allotted lands could not, under the rule of liberal construction rightly invoked by the petitioners, be deemed excluded from the benefits of the exemption granted." The Court rejected the view that the tax was on the royalty after it was produced, and therefore on personalty.

17. Notes 14, 15, 16.

In Dawson v. Kentucky Distilleries, 255 U. S. 288, 291, it was said: "The attorney general concedes that the tax, if a property tax, is invalid since it does not comply with the requirements of a property tax specified in * * * the State Constitution. * * * He contends * * * that the tax is * * * a license tax upon 'the business of' * * * owning and storing * * * 'spirits in bonded warehouses.'" The Court held the law imposed a property tax and as such was concededly invalid, agreeing that the thing really taxed "is the act of the owner in taking his property out of storage into his own possession * * * for the purpose of making some one of the only uses of which it is capable * * * To levy a tax by reason of ownership of property is to tax the property."

THIRD: It has never been supposed that a community of interest or reciprocal relation arose between a grantor and grantee, because the consideration for the grant of a freehold estate was payable in installments, or in a particular way, or was reserved as rent, or because the grant was limited to a specified use, or was upon a limitation or condition.

Would a villein be held to have become engaged jointly with his lord, because he held by rent service?

Would a landlord of this day, renting on shares, furnishing the teams, seed, etc., be engaged in a common enterprise with his tenant?

Would a landlord who erected a building for the special use of his tenant, reserving as rent a share of the profits, be engaged in a common undertaking with the tenant?[18]

Would a lender of money, who reserved a share of the profits of a particular enterprise, in lieu of interest, be engaged in a joint venture, with the borrower?[19]

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18. **"An agreement that the lessor of a hotel shall receive a certain portion of the profits therof by way of rent does not make him a partner with the lessee." Meehan v. Valentine, 145 U. S. 611, 623-4.**

19. "The partnership relation does not exist where the interest in net profits is by way of compensation or remuneration for: (1) services as clerk or other employee (Goode v. McCartney, 10 Tex. 193); (2) commission as agent or broker (Buzard v. Bank, 67 Tex. 83, 2 S. W. 54, 60 Am. Rep. 7); (3) *rental for property real or personal* (Fink v. Brown (Tex. Com.

Surely, the intention of the parties is controlling, even if a question of taxation is involved.[20] The lessee contracts with the lessor because he is in, or wants to get into the business of producing oil—not because he intends to engage in it with the lessor.

A careful search has failed to disclose a single case or text in which it was even contended that there was anything in the nature of a joint purpose in the minds of the grantor and grantee of an oil and gas lease.

Landlord and tenant and vendor and vendee,[21] ten-

App.) 215 S. W. 846); (4) *interest on money loaned* (Kelly Island Lime & Transport Co. v. Masterson, 100 Tex. 38, 93 S. W. 427, 430)" Gardner v. Wesner, 55 S. W. (2) 1104 by the Chief Justice of the Texas Court of Civil Appeals from whence this appeal came.

20. "The true rule * * * would seem to be that the agreement and intention of the parties themselves should govern in all the cases. If they intended a partnership in the capital stock, or in the profits, or in both, then that the same rule should apply in favor of third persons, even if the agreement were unknown to them. And on the other hand, if no such partnership were intended between the parties, then that there should be none as to third persons, unless where the parties had held themselves out as partners to the public, or their conduct operated as a fraud or deceit upon third persons." Meehan v. Valentine, 145 U. S. 611, 623-4.

21. After the production of oil, "the relation of landlord and tenant, or vendor and vendee is established." Mills & Willingham, Law of Oil & Gas, p. 72, citing Glasgow v. Chartiers Oil Co., 152 Pa. 48, 25 Atl 232, Venture Oil Co. v. Fretts, 152 Pa. 451, 25 Atl., 732.

ants in common,[22] and co-tenants[23] they have been called, but joint venturers, common owners of the business of producing, partners or mining partners—never.

But it has often been decided that a co-owner of a part of the *working interest* in an oil and gas leasehold, even though he holds under the lessee and must share in the expense of operation is not jointly engaged in the business of producing, by reason of title alone[24]—and this is in line with the cases here.[25] It

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22. Taylor v. Higgins Oil & Fuel Co., 2 S.W. (2) 288, 295.

But in Mills & Willingham "Law of Oil & Gas." p. 264 it is said that:

"The lessor and lessee of an oil and gas lease, however, are not tenants in common. The lessor, while he has the right of possession and other purposes has parted with the right of possession for the purpose of producing oil and gas, to the lessee, who is substituted in his place, consequently there is no UNITY of possession between them."

23. Gardner v. Wesner, infra pp. 20-22.

24. Notes 25, 27, 37, 38, 39.

In Bolding v. Camp, 6 S. W. (2) 94, 96, Bolding bought and paid for a 1/16th interest in an oil lease. It was contended he was a partner because he would thus be liable for a share of the expenses of operation; but the Court said: "The agreement on its face is one of tenancy in common. * * * It is urged that sharing of profits was contemplated. The evidentiary predicate is the purchase of the 'one-sixteenth interest' in the leasehold. * * * It might well be that Bolding bought a one-sixteenth part of the minerals in place; whatever inference lies is (we

25. Note 25 commences on page 22.

is only when there has been an engagement for ac-

think) to that end for whatever the nature of the leasehold he acquired that aliquot part of realty. * * * True it is, he might be charged, under given circumstances with a portion of the expense of severance, but the requisite circumstances are not shown and the charge hypothetized would arise in virtue of tenancy in common, and not because of partnership."

In 31 Texas Jurisprudence pp. 538-9, it is said: "When land containing oil and gas is owned by two or more persons in common, any one of them may extract the minerals regardless of co-operation by the others in the undertaking. If the other owners decline to participate, the producer cannot compel them to contribute to his enterprise; he must rely upon his own resources, and if he fails, he alone must bear the loss. On the other hand, if oil or gas is produced in paying quantities, the producer must account to the other owners for its value, after the costs of production and marketing have been deducted."

In Mills & Willingham "Law of Oil & Gas" pp. 274-275, it is said that:

"There is no relation of partnership, nor presumption of it, from co-tenancy itself, in a mine, or in an oil and gas lease. It arises only when the co-tenants actually begin operating the joint property. * * * There is a distinction in principle between the mining of solid minerals, and the production of oil and gas, in that in the case of oil and gas 'the production may be and usually is delivered to the pipe line and credited to each co-tenant, without ever having become a part of the social assets. * * * In which event there is no division of the profits and losses, as between the co-tenants * * * nor are there any social assets, unless jointly owned equipment could be so considered."

Dunnigan T. & S. Co. v. Carroll, 60 S. W. (2) 296, by the same judge who wrote the opinion of the Court

tual participation in the management of the prop-

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of Civil Appeals in this case, involved the question whether a contract between the owner of an oil lease and a driller, for the drilling of oil wells in part consideration for which the owner assigned a one-sixteenth interest in the lease, constituted a mining partnership. The Court said:

> "The manifest purpose of the drilling contracts was to obtain the drilling of certain oil wells for a certain stipulated consideration or compensation. They evidence no agreement of a joint undertaking or agency to operate the leases, and to share profits as such, but the contrary is clearly evidenced by the contract with Morgan, in that it provided that the specified interest to be assigned Carroll in the leases, or the specified amount of oil to be credited as a part of the compensation to him for drilling the first two wells. * * *
>
> "It is therefore manifest that a mining partnership, as that relationship has been defined in law *as arising from joint operations and sharing of profits as such*, was not shown in this case; but *the contracts* themselves clearly *show* that *the parties contracted for the drilling of certain oil wells for a stipulated consideration, and not in consideration of sharing profits as such, or joint operation of a mining enterprise.* * * *
>
> "In the recent case of Gardner v. Wesner (Tex. Civ. App.) 55 S. W. (2) 1104), 1106, * * * it was held that the joint ownership of the mining property will not alone create a mining partnership; but that, as was held in the cases of Wagner Supply Co. v. Bateman, 118 Tex. 499, 18 S. W. (2) 1052; Munsey v. Mills, 115 Tex. 469, 283 S. W. 754, and the other cases cited, 'joint operation, sharing of profits, community of interests, and the mutual agency' must also be

erty that the owners have been held to be mining

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shown in order to constitute a mining partnership. The Gardner Case further held that the mere 'sharing in net profits of mining venture does not create relation of mining partner,' and especially so where the terms of the agreement show the profits were paid as compensation for services rendered."

Gardner v. Wesner, 55 S. W. (2) 1104, by the Chief Justice of the Court from which this appeal came, involved the question whether a mining partnership existed between the owner of a lease who contracted for cleaning a well in part consideration for which it was agreed that the well cleaner should receive a one-eighth of the net profits from the well if it produced. The Court said:

"In order to constitute a mining partnership **(sometimes called a joint venture)** there must be not only a joint ownership of the mining property (which of itself creates only the relation of cotenancy), but also a joint operation. 'The actual working of the mine by the joint owners is essential to a mining partnership.' 22 A. & E. Ency. of Law, p. 228. This rule is so well established as to be now regarded as elementary (40 C. J., p. 1145; 18 R. C. L. p. 1200, Sec. 106; 2 Thornton's Oil & Gas (5th Ed.) Secs. 658-667; Summer's Oil & Gas, Sec. 235), and has been followed in this state whenever the question has been presented. Bolding v. Camp (Tex. Com. App.) 6 S. W. (2) 94; Leath v. Benton Abstract & Title Co. (Tex. Civ. App.) 9 S. W. (2) 501; Lowry Oil Corp. v. Bennett (Tex. Civ. App.) 16 S. W. (2) 947; Ferguson v. Rhoades Drilling Co. (Tex. Civ. App.) 271 S. W. 155; Adams v. Texhoma O. & R. Co. (Tex. Civ. App.) 262 S. W. 139.

"The Texas cases in which it has been held that

partners.[26] Where the question whether a partner-

a mining partnership existed presented the elements 'not only a joint ownership of the lease * * * but joint operation, sharing of profits, community of interests, and the mutual agency * * * in the management of the lease and exploration for oil.' Wagner Supply Co. v. Bateman, 118 Tex. 499, 18 S. W. (2) 1052, 1055; Munsey v. Mills & Garitty, 115 Tex. 469, 283 S. W. 754; Mayfield v. Key (Tex. Civ. App.) 260 S. W. 926; Indiahoma Ref. Co. v. Wood (Tex. Civ. App.) 255 S. W. 212.

"That sharing in the net profits of a mining venture does not create the relation of mining partner, was held in the early Colorado case of Le Fevre v. Castagnio, 5 Colo. 564. * * *

"The holding in that case has been uniformly followed in mining partnership cases, so far as we have been able to discover. The following Texas cases are directly in point: Lowry Oil Corp. v. Bennett (Tex. Civ. App.) 16 S. W. (2) 947; Leath v. Benton Abstract & Title Co. (Tex. Civ. App.) 9 S. W. (2) 501 (error dis.)

"In the law of partnership generally, the net profits rule, which at one time prevailed in England, has never been adopted in this state; although some expressions in Cochran v. Marmaduke, 60 Tex. 370, led to some confusion for a while, as to what exceptions to the rule should be applied. Fouke v. Brengle (Tex. Civ. App.) 51 S. W. 519; Rahl v. Parlin & Orendorff Co., 27 Tex. Civ. App. 72, 64 S.W. 1007. The decision in that case has been clarified by subsequent holdings of the Supreme Court, and it is now generally recognized in this state that to constitute a partnership there must be: 'A community of interests, the common enterprise, its

26. Note 26 is on page 23.

ship exists has been raised between co-owners of the

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operation for the joint account, and a right in the owner of each interest to share as a principal in its profits as such, which under the established rule in this state is a recognized test of the relation.' Freeman v. Huttig Sash & Door Co., 105 Tex. 560, 153 S. W. 122, 125, Ann. Cas. 1916E, 446.

"Specifically, it has been held that the partnership relation does not exist where the interest in net profits is by way of compensation or remuneration for: (1) services as clerk or other employee (Goode v. McCartney, 10 Tex. 193); (2) commission as agent or broker (Buzard v. Bank, 67 Tex. 83, 2 S. W. 54, 60 Am. Rep. 7); (3) *rental for property, real or personal* (Fink v. Brown (Tex. Com. App.) 215 S. W. 846); (4) interest on money loaned (Kelly Island Lime & Transport Co. v. Masterson, 100 Tex. 38, 93 S. W. 427, 430). * * *

"Conclusions from the authorities are summarized on pages 1105, 1106 of 18 L. R. A. (N. S.), one of which we quote: '*When the profit sharer is simply* an agent or servant, *one who furnishes property*, a lender of money, or a mere creditor, *who receives the profits as compensation for his services, for the use of his property* or money, or in order to collect his debt, *without more, he is not liable as a partner*, and the presumption is overthrown.'"

25. "The fact that real property is held in the joint names of several owners, or in the name of one for the benefit of all, is no evidence of co-partnership between them with respect to it. In the absence of proof of its purchase with partnership funds for partnership purposes, real property standing in the names of several persons is deemed to be held by them

working interest, and nothing but the fact of ownership has been shown, the cases have sometimes pointed out that they sustain more nearly the relation of lessor and lessee and are not mining partners.[27] **In all the cases, it is held that a joint venture cannot**

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as joint tenants or as tenants in common, and none of the several owners possesses authority to sell or bind the interest of his co-owners." Thompson v. Bowman, 6 Wall. 316, 317.

See Notes 3, 18 supra.

26. Notes 19, 24, 27, 39, especially Gardner v. Wesner, 55 S. W. (2) 1104, pages 20-22, supra.

27. "The rule is that a mining partnership arises by operation of law where co-owners work a mine. * * * The clause in the contract that Bateman's one-fourth interest 'is to be held as royalty interest' plainly shows that, as between the owners, his interest was to be free of cost to him, as royalty is ordinarily free of cost to the owner. The property rights, however, of Bateman, were not those of a royalty owner. He was not the original owner of the lease or the entire estate in the land, and he bought no royalty interest from anyone. Royalty is usually the amount reserved or the rental to be paid the original owner of the whole estate, and Bateman's interest does not come within the usual and ordinary signification of the term." Wagner Supply Co. v. Bateman, 18 S. W. (2) (Tex. Sup.) 1052.

Lowry Oil Corporation v. Bennett, 16 S. W. (2) 947, involved the question whether the defendants, each of whom "owned an undivided interest in an oil lease on the land mentioned above, and each was entitled under an agreement with the other co-owners, to a proportionate part of the net profits derived from the drilling of a well upon the land" were partners. The Court said:

exist when the profits are not shared as such, when there is no community of management, and where the profits are rendered as compensation for the use

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"Notwithstanding the fact that after the Lowry Oil Corporation became the owner of the interests in the lease it would be entitled to share in the profits arising from the development of the lease, yet, under the undisputed facts recited above, it could not be held liable as a partner with Ferguson for the oil purchased by the latter Bolding v. Camp (Tex. Com. App.) 6 S. W. (2) 94; Fink v. Brown (Tex. Com. App.) 215 S. W. 846, and authorities there cited—all to the effect that the rule that a mere sharing in the profits fixes the relation of partnership does not obtain in this state. Ferguson v. Rhoades Drilling Co. (Tex. Civ. App.) 271 S. W. 155; Humble Oil & Refining Co. v. Strauss (Tex. Civ. App.) 243 S. W. 528; Mills & Amsterdam Cas. Co. v. Harrington (Tex. Civ. App.) 11 S. W. (2) 533 (writ of error dismissed). * * *

"With respect to the question of partnership growing out of that transaction, in principle, Jackson's relation to the development of the lease as a result of Ferguson's contract with him to convey him a one-sixteenth interest in it and to drill the well thereon, for the consideration of hauling the rig, *was not different from that of the owner of land who conveys an interest therein in the way of an oil lease, and in consideration therefor the lessee agrees to develop the lease for oil and gas and to pay the lessor a one-sixteenth or some other portion of the oil, which, under authorities cited above, would not create a partnership relation between the lessor and lessee.*"

of money, property, chattels, services, and the like.[28]

FOURTH: Considering the lessor's interest under a lease as rent, it becomes perfectly clear that the doctrine of implied covenants to which reference has been made has to do with the lessor's right to rent and does not alter the relation between the parties. Under this doctrine the lessor is entitled to rent within a reasonable time and in a reasonable amount, whether the lessee produces oil or not.[29] This right to full compensation for the rights and privileges granted to the lessee, has none of the incidents which

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28. Notes 19, 24, 27, 39, Gardner v. Wesner, pages 20-22 supra.

29. "Where a mining lease provided for oil or gas royalties, and failed to define the lessee's duty as regards development after discovery of oil or gas, the law implied the obligation from the lessee to continue the development and production of oil or gas with reasonable diligence. * * *

"The usual remedy for breach of the lessee's implied covenant for reasonable development of oil and gas is an action for damages. * * *

" 'So long as the sulphur company breaches or violates its contractual duty to operate one plant, the royalty company may recover its compensation for the full amount of sulphur that should have been produced as contemplated by the contract.' (Freeport Sulphur Co. v. American Sulphur Royalty Co., 6 S. W. (2). * * * "The true basis of the whole doctrine of implied covenants in oil and gas leases may be found in the determination of courts to enforce fair dealing between lessor and lessee which could not otherwise be assured." Waggoner Estate v. Sigler Oil Co., 19 S. W. (2) 27, 29.

attend the commitment of one man to another in common purpose.

FIFTH: Oil leases are bought by persons and corporations engaged in the business of producing oil. Their activity in the business is not an appurtenance or franchise which exists by virtue of the ownership of any particular lease. It is a right that exists and has its value, entirely distinct and independent of the ownership of a lease.[30] The lease comes into the picture as a part of the means by which the business is conducted.

The lease is not put into a common undertaking, with the lessee, it is outright sold and granted. The lessor's reserved rights are subject to sale in various ways. He may grant a fraction of the reversion, a part or all of the royalty on a part or all the land affected by the lease, a part of the delay rentals or bonuses on present or future leases, and under Sheffield v. Hogg, all these are real property. Such grants carry with them the entire interest of the lessor, as far as they go. Glassmire[31] estimates that one-half million individuals and companies in the United States are the owners of petroleum royalty interests. These interests are often so divided that an interest holder is entitled to no more than one out of every million and a half barrels of oil and it is not uncommon to see more than two hundred royalty owners under a single lease.

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30. Note 16 supra.

31. Glassmire Law of Oil & Gas Leases and Royalties (1935) p. 54.

The tax in question falls on all these interests and people, regardless of where they reside—some even in foreign countries—thousands who were never in the State of Texas and never saw an oil field. Yet, they are declared to have intended to engage in a joint venture in this State, solely by virtue of a grant of real property.

A part of the Cook Estate royalty was put into an endowment fund for a hospital; and the hospital is declared to be engaged in a mining venture.

Large royalties are held by corporations, restricted Indians, banks, minors, insane persons, Trust Companies, schools, lawyers and judges, and they are all declared to be committed to a common undertaking with the producer of their oil.

On the basis of one million barrels per day production, which is a low average, the tax on royalty owners in Texas, exceeds Nine Hundred Thousand Dollars per annum.

SIXTH: While we agree and argued that the Court of Civil Appeals intended to hold the law laid an excise on the production of oil—an occupation tax under our Constitution[32]—WE KNOW IT DID NOT INTEND TO OVERRULE ALL THE DECISIONS BY WHICH THE LESSOR-LESSEE RELATION HAS BEEN ESTABLISHED TO BE THAT OF GRANTOR AND GRANTEE OF A FREEHOLD

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32. Note 16 pp. 12-14, supra.

ESTATE[33] IN WHICH THE GRANTOR RESERVED A RENT AS CONSIDERATION FOR THE GRANT,[34] **and all the cases defining mining partnerships and common ventures**—the best of which it decided itself only a short time ago[35]—which have been extensively quoted from in the notes set forth in this petition. These decisions, coupled with the entire absence of any considered authority holding the lessor and lessee are engaged in a common enterprise or mining venture by virtue of the terms of an ordinary oil lease, conclusively demonstrate that they are merely grantor and grantee—and this is so well understood in all the oil fields and in Texas that it is but rule of thumb law. We predict a decision to the contrary will never be followed when an issue arises between the lessor and lessee or third persons, as to the intent and construction of an oil lease. Surely out of the myriad of cases where this and analogous relations have been involved, a lessor or grantor would have long ago been put in the category of a partner if it had been imagined he was such. Countless times an eye has been longingly cast in his direction when a lessee failed and left unpaid

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33. Notes 5, 10, 21, 27, 39.

34. Notes 7-11, 18, 19, 21, 22, 24, 27, 38, 39.

35. Notes 18, 19, 24, especially Gardner v. Wesner, supra, pp. 20-22.

claims, and sometimes a lien has been sought against his interest, with no avail.[36]

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Thus, the case comes back to the argument we originally submitted. The Court of Civil Appeals simply attempted to justify an excise because of the ownership of property.

While the Court of Civil Appeals said that one of the purposes of the lease was the future development and operation of the lease for oil, in accordance with its terms, for the "mutual benefit" of the parties, it **certainly did not say that this "mutual benefit" resulted from joint operation of the prop-**

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36. "Ordinarily one can only subject to a lien such interest in real property as he may have. So the lessee subjects the lease to a lien, but the lessor's reversion is in no way involved. Mills & Willingham "Law of Oil and Gas," p. 346.

"So the lessee is not the agent of the lessor for development of the lease and the lessor is not personally liable to laborers and materialmen." Id. p. 348, citing Thompson v. Hickman, 262 S. W. (Ark) 20, which holds that neither the lessor personally, nor his reversionary interest are liable to pay employees of the lessee where he does no more than accept the benefits accruing to him under an oil and gas lease.

And when the lease ceases to exist, the lien also dies. Kelley v. Shamburger Lumber Co., 23 S. W. (2) 883.

erty—which is indispensable to a joint venture.[37] What it meant was that development of the lease would result in such benefit or profit as any ordinary contract contemplates.

Nor did the Court hold that the oil produced was shared or divided as profits of an enterprise; indeed, it could not dispute the many holdings that so far as the lessor's interest is concerned **it was deliverable as compensation for the granted privileges.**

"The *consideration* moving to the lessor (as rent for the grant of a freehold) is an *interest* in the oil or its value in money." But, the *consideration* was payable as rent for a grant, and is real property;[38]

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37. Notes 18, 19, 24, 25, 27, 39. In Gardner v. Wesner, supra, the Court said: "In order to constitute a mining partnership (**sometimes called a joint venture**) there must be not only a joint ownership of the mining property (which of itself creates only the relation of co-tenancy) *but also a joint operation.* 'The actual working of a mine by the joint owners is essential to a mining partnership.' "

38. Notes 7, 8, 9, 10, 11, 14, 15, 24, 39.

"Thus, if a party has no interest whatsoever in the capital stock and as between himself and the other parties, has also no rights as a partner, or no mutuality of powers and duties, but is simply employed as an agent, and is to receive either a given sum out of the profits, or a proportion of the profits, or a residium of the profits, beyond a certain sum, as a compensation for his labor and services as agent of the concern, and not otherwise; he will not be deemed a partner in the concern from the fact alone; nor a partner with the others inter sesse, for that would be contrary to their intentions and objects, nor

not "mutual profits" or a "mutual" sharing of the oil. The fact we receive part of the oil as compensation for a grant of our land is no evidence that we have a community of interest in the production of oil on it.[39] Thus the indispensable elements of a

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as to third persons, because the transaction admits of a different interpretation, and may justly be deemed a mere mode of ascertaining and paying the compensation of an agent, as in a naked case of agency. *In such a case it may be properly enough said that the agent is entitled to a share or portion in the profits, liquidated or unliquidated and therefore that he has in a certain sense a community of interest therein, with the actual partners. But he does not participate therein as an owner pro tanto, or as possessed thereof per my et per tout, or as clothed with the rights and powers and duties of a partner.*" Story on Partnership, Sect. 32.

" 'In order to constitute a communion of profits between the parties, the interest in the profits must be mutual, that is, each person must have a specific interest in the profits, *as a principal trader*. He is not a partner if he merely received out of the profits a compensation for his trouble, in the character of an agent or servant of the concern.' " Story on Partnership, Sect. 33.

39. Notes 5, 7, 10, 38.

"Mining partnerships by operation of law are based on *joint ownership* and *joint operation* of the mineral estate. There must be an existing mineral work and operation; joint ownership of the land alone is not enough." 32 Tex. Jurisprudence, p. 246.

"The ultimate fact to be shown is common ownership of the business and its profits; but the conclusion that a partnership is disclosed does not follow

joint venture are lacking.[40]

The lessor's "interest in the success of the business"

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as a matter of law from proof of joint interest in a contract and a right to share profits." Id p 245.

"Common ownership of chattels or of land does not amount to a partnership between the owners. Id. p. 252.

"A lease ordinarily does not create between lessor and lessee, contrary to their intention, a partnership because it reserves a share of ultimate net profits from operation of the leased plant and business for which a fixed rental is to be paid in any event. Nor does a partnership exist by reason of a lease of space in a department store for a percentage of net sales which designates the parties as lessor and lessee and which creates no community of interest. Id. p. 259.

"In a tenancy in common each party has a separate and distinct, although an undivided interest, and possesses (as it is technically expressed) the whole of an undivided moiety of the property, and not an undivided moiety of the whole property; whereas in partnership the partners are joint owners of the whole property. Story on Partnership, p. 134.

"In every case of partnership there is a community of the property of the partnership between the parties as soon as it becomes part of the common stock. * * * Partners therefore are to be treated * * * as * * * having an interest * * * in, and the entire possession, as well of every parcel, as of the whole. This principle * * * seems to result directly from the nature of the contract of partnership, which supposes, that the property brought into it is put into community by the joint consent of the parties. Story on Partnership. Sects. 15-16-17.

40. Note 24.

is economic, and not joint or of a community character. We are all interested in the success of the business of those with whom we contract, especially if they covenant to do us an independent service that we are prohibited from doing by the same contract. We would have a different interest in a common business, for under Texas law, having a joint right in the whole, we would have something to do with its success.[41]

The right to enforce the duty of a lessee to pay rent whether upon the express or the implied terms of the lease,[42] is a property right and denotes the opposite of joint or common working of an oil well. If the operation were joint there could be no such thing as an implied covenant upon the part of the lessee to reasonably develop and produce, as both the lessor and lessee would then be responsible for the failure to enlarge the activity.[43]

The reason the Court of Civil Appeals did not say the lessor and lessee were joint venturers is thus readily apparent from its own decisions and the common law of oil and gas. NOTHING IN COMMON BETWEEN THE LESSOR AND LESSEE REMAINS BUT COMMON OWNERSHIP OF THE OIL AND A DUTY TO PAY RENT.—THESE ARE PROPERTY.

The tax is in truth upon the lessor's rent and not

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41. Note 24.

42. Note 22, 24, 37, 38, 39.

43. Note 29.

upon the production of oil; it falls upon those who have interests in the oil produced, solely by reason of their interests and not because of any joint share or common purpose in the production, or common or mutual benefit therefrom.

The New Mexico case, Flynn v. State Tax Commission, 23 Pac (2d) 889, 892, assumes an element which is not present in this case, in the *dicta* quoted in the opinion, when it says that the lessee and royalty owner "*considered as participating in a joint enterprise*, are both engaged in the business of producing oil." Of course, assuming that it was shown they were jointly engaged in producing oil, the result is correct, for there is nothing in their relation to prevent them agreeing upon joint operation or engaging in a joint venture. We think from the whole opinion in that case the Court meant to say that if it were shown that they jointly operated the property they would be liable for the tax as producers, but that it was unnecessary to determine the question. In view of the long established principles set forth in the notes hereto it should require more than dicta to convince one that there is anything in an ordinary oil lease which creates the relation of joint venturers between the lessor and lessee therein.

The Supreme Court of Louisiana reached the correct result in State v. Stiles, 68 So. 947, when, interpreting a similar law it said that: "Article 229 of the Constitution does not provide for imposing a license tax upon the land or royalty owner, but only *upon those engaged in the business of severing natural resources from the soil.* * * * Our conclusion is that the expression in the second section of the stat-

ute, 'less the royalty interest accruing to the owner thereof, merely deprives the state of so much revenue; and that the proceeding clause *'the license on which shall be paid by said land or royalty owner'* has no effect whatever. *If the Legislature had undertaken to impose this license tax upon land or royalty owner, NOT ENGAGED IN THE BUSINESS OF SEVERING NATURAL RESOURCES FROM THE SOIL, it would have been without any constitutional authority."*

Having, as we believe, shown beyond all doubt that this Honorable Court did not correctly interpret the meaning of the Court of Civil Appeals; that the opinion of the Court below merely evaded the issue,[44] and that under the settled law relating to oil and gas,[45] the excise falls directly on our property rights and not on any privilege we have in relation to the production of oil, we respectfully submit that the law in question arbitrarily ignores substantial facts when it declares the owners of royalty interests in the oil produced to be engaged in the business of producing oil, and that the sole object of the law was to increase the income of the lessee and decrease that of the lessor proportionately, in the guise of an excise, or occupation tax, as it is called, under our Constitution.

Respectfully submitted,

WILLIAM R. WATKINS,

Attorney for Appellants.

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44. See our original Brief pp. 21-27.

45. B & W Taxi Co. v. B & Y Taxi Co, pp 57-59 our original Brief.

This petition is presented in good faith and not for delay.

WILLIAM R. WATKINS,
Attorney for Appellants.

SUPREME COURT OF THE UNITED STATES.

No. 10.—October Term, 1936.

Joseph H. Barwise and George Thompson, Jr., as Trustees of the Estate of Mrs. M. M. (W. I.) Cook, Deceased, Appellants,
vs.
George H. Sheppard, as Comptroller of the State of Texas, et al.

Appeal from the Court of Civil Appeals, Third Supreme Judicial District, State of Texas.

[November 9, 1936.]

Mr. Justice Van Devanter delivered the opinion of the Court.

A statute of the State of Texas imposing a tax on the production of oil is here challenged as violating the contract clause of the Constitution of the United States and the due process of law clause of the Fourteenth Amendment.

The appellants own lands from which oil is produced under a lease given in 1925. The lease is in the usual form of an oil lease; invests the lessee with the right to explore for and produce oil; shows that the production is to be for the mutual benefit of the lessor and lessee; fixes the lessor's proportion, or royalty interest, at "the equal 1/8 part of all oil produced"; and requires the lessee to deliver that proportion to the lessor's credit, "free of cost, in the pipe line" to which the wells are connected.

When the lease was given and up to 1933 a law of the State imposed on the lessee alone, as the active producer, a tax on all oil produced,[1] and that tax was paid and borne by the lessee so long as that law remained in force.

By an act of 1933 [2] a substituted tax on oil production was imposed with an accompanying provision that the tax "shall be borne ratably by all interested parties including royalty interests" and with other provisions designed to secure prompt and certain payment of the full tax as by charging the active producer, or the

[1] Vernon's Ann. Tex. Stat., Art. 7071.

[2] Act 1933, Reg. Sess., c. 162, § 2, as amended by Act 1933, 1st Called Sess., c. 12.

purchaser of the oil where sold in the pipe line, with a primary duty to pay the full tax, and authorizing and requiring him to withhold from royalty or purchase money due interested parties the proportionate tax due from them.[3]

For about a year after the act of 1933 became effective the purchaser of the oil produced under the lease paid the full tax and deducted the appellants' proportion from what was due to them on the purchase of their share of the oil. The payment of this part of the tax was accompanied by written protests of the appellants and the purchaser.

The present suit was brought by the appellants against the Comptroller and Treasurer of the State to secure a refund of the taxes paid under protest and an injunction against the collection of further taxes in respect of appellants' interest in the production. In the court of first instance there was a decree for the defendants, which the Court of Civil Appeals affirmed after sustaining the taxing act against appellants' before mentioned challenge to its validity.[4] The Supreme Court of the State declined to take the case on writ of error, and an appeal to this Court was sought and allowed.

We come first to the contention that, as applied to the appellants, who are not actively engaged in the production of oil but are lessors having a royalty interest, the act is an arbitrary fiat, in contravention of fundamental principles of private right and distributive justice, and therefore denies to appellants the due process of law guaranteed by the Fourteenth Amendment.

The taxing act calls the tax an "occupation tax" and a "gross production tax". The Court of Civil Appeals applies to it both of these designations, and also characterizes it as a "tax levied on the business or occupation of producing oil". In discussing appellants' claim that they are not engaged in such a business or occupation and that the act nevertheless includes them among those on whom the tax is laid, the court expresses the view that, for the purposes of such a tax, "the legislature may validly declare the

[3] Section 2 (3) provides: "The purchaser of oil shall pay the tax on all oil purchased and deduct tax so paid from payment due producer or other interest holder. . . .".

And section 2 (6) further provides: "The tax herein levied shall be borne ratably by all interested parties, including royalty interests; and producers and/or purchasers of oil are hereby authorized and required to withhold from any payment due interested parties, the proportionate tax due".

[4] 89 S. W. (2d) 1026.

owners of royalty or other interests in the oil produced to be engaged in the occupation or business of producing oil". The designations applied to the tax and the view just noticed are stressed by counsel for the appellants and relied upon as supporting the contention that the taxing act is essentially an arbitrary fiat.

But when mere characterizations of the tax are put aside and attention is given to the substance of the court's opinions in this and a companion case,[5] it unmistakably appears that the court regarded the tax as an excise laid on the production of oil, measured by the extent of the production, and charged ratably against all who have an interest in the oil produced. True, the court speaks of the tax as laid on the "occupation or business" of producing oil, but its opinions plainly show that these terms are used in the sense of a "planned undertaking" or "mining venture" and as comprehending all who have a direct and beneficial interest in the oil being produced, whether they be owners conducting oil operations on their own lands, or lessees operating under leases from owners and sharing the oil with the latter, or owners who have leased their lands for oil operations and share the oil with the lessees. As illustrating the actual decision and the reasons underlying it we quote from the opinions:

"The legislative intent to levy the tax ratably against all interested parties in the oil produced is also clearly evidenced by the language that 'the purchaser of oil shall pay the tax on all oil purchased and deduct tax so paid from payment due producer or other interest holder,' and 'withhold from any payments due interested parties, the proportionate tax due.' These provisions do not levy the tax against the purchaser. He is merely made the agent of the State to collect from the producer or other interest holders the total amount of the tax due; and he is authorized to charge their respective accounts with 'the proportionate tax due.' That is, the purchaser withholds from the producer only as an interest holder and only to the extent of his interest. Likewise the purchaser withholds from other royalty or interest holders the amount of the tax due on their royalty or other interests. The Act, therefore, designates the parties against whom the tax is levied. The amount of the tax due by each is also defined or measured by the extent of interest in the oil produced, or the amount paid because it was produced."

. . . . . .

"It is also manifest that the tax is not dependent upon the character of title under which the producer produces the oil. Nor

[5] Group No. 1 Oil Corporation *v.* Sheppard, 89 S. W. 1021.

is the tax levied on the oil in place. The tax is levied on the business or occupation of producing the oil."

"The ordinary form of oil lease has a dual character or purpose: (1) the conveyance of an estate in the land for development purposes; and (2) the future development and operation of the lease for oil in accordance with the terms, express and implied, of the contract for the mutual benefit of the parties, their respective benefits being measured by the extent of their interests in the oil produced, or its value. The law is settled that the primary objective or purpose of the oil lease is the production of oil for the mutual profit of the parties. The consideration moving to the lessor is an interest in the oil or its value in money. Thus he has a direct interest in the success of the business. As the holder of the royalty interest the lessor or royalty owner is not only entitled to share in the gross production of the oil, but may under the terms of the lease, expressed or implied, require proper, prudent and diligent management and development of the business, and has reserved and is entitled to both legal and equitable remedies necessary to enforce the obligations of the lease, and under some circumstances may forfeit the lease for non-development."

And the court quoted the following from a decision of the Supreme Court of New Mexico:[6]

"Our minds do not reject the idea that the lessee and the royalty owner, considered as participating in a joint enterprise, are both engaged in the business of producing or severing oil, and that the tax is therefore essentially occupational. Such a view, however, is not indispensable to sustaining the tax. For it may be considered occupational as to the lessee, and another kind of tax to the royalty owner. Unless found as to one or the other, to be a tax upon tangible property, it need not be levied ad valorem, and is an excise."

In view of this exposition of the purpose and meaning of the act, we are of opinion that it is not an arbitrary fiat and does not infringe the due process of law clause of the Fourteenth Amendment.

While operations under the lease are carrried on by the lessee and not by the lessors, they nevertheless are carried on in virtue of the lease, that is to say, under stipulations made between the lessors and the lessee. The lease shows that the parties to it are, in a very practical sense, committed to and engaged in a common venture for their mutual benefit. The lessors have put into the venture

[6] Flynn v. State Tax Commission, 28 Pac. (2d) 889, 892.

their right to explore for and to extract the oil under their lands, and the lessee has put into it various drilling and pumping appliances and much expense, labor, and time. All that has been put in is devoted to the common purpose of producing oil in which the lessors and the lessee are to have stated interests. It is this production that is taxed against the lessors and the lessee according to their respective interests.

Without question the State has power to lay an excise on the production of oil. Here it is laid, admissibly we think, on those having a direct and beneficial interest in the oil produced and is apportioned between them according to their interests. The apportionment is reasonable, not arbitrary; and is as reasonable to the lessors as to the lessee.

We come next to the contention that the act, in so far as it imposes the tax on the appellants, impairs the obligation of their contract with the lessee whereby he agrees to deliver to their credit, "free of cost", in the pipe line, the equal 1/8 part of the oil produced. The lease contains no mention of taxes or of their payment. It well may be that when rightly construed, the engagement to deliver, free of cost, refers to expenses incurred in producing the oil and conducting it to the pipe line, and is not intended to include governmental exactions, such as a tax. This would appear to be an admissible if not a necessary construction of that engagement. But, be this as it may, the lease was made in subordination to the power of the State to tax the production of oil and to apportion the tax between the lessors and the lessee. The taxing act does not purport to reach or affect any term of the lease. Plainly no stipulation in the lease can be of any avail as against the power of the State to impose the tax, prescribe who shall be under a duty to the State to pay it, and fix the time and mode of payment. And this is true even though it be assumed to be admissible for the lessors and lessee to stipulate as to who, as between themselves, shall ultimately bear the tax. These views are but a reiteration and application of what repeatedly has been held in respect of contracts and their subordination to the taxing power.[7]

[7] Providence Bank *v.* Billings, 4 Pet. 514, 562; North Missouri R. R. Co. *v.* Maguire, 20 Wall. 46, 61; Moffit *v.* Kelly, 218 U. S. 400, 403; Henderson Bridge Co. *v.* Henderson City, 173 U. S. 592, 619-620; Chanler *v.* Kelsey, 205 U. S. 466, 478-479; Kehrer *v.* Stewart, 197 U. S. 60, 70; Clement National Bank *v.* Vermont, 231 U. S. 120, 143; Lake Superior Consolidated Iron Mines Co. *v.* Lord, 271 U. S. 577, 581.

It is true that the law in force when the lease was made and for some years thereafter laid a production tax on the lessee alone, and it is equally true that under the act of 1933 a part of the tax is imposed on the lessors and the part imposed on the lessee is less than what would fall on him under the earlier law. But the State's power in the matter was in no way circumscribed by the earlier law. That law was subject to change at any time through a further exertion of the taxing power; and the lease presented no obstacle to such a change.

It follows that appellants' reliance on the contract clause of the Constitution is ill-grounded.

Decree affirmed.

A true copy.

Test:

Clerk, Supreme Court, U. S.